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No. 97-

In The

Supreme Court of the United States

October Term, 1996

FIREMAN'S FUND INSURANCE COMPANY, INC.

Petitioner,

vs.

PAINEWEBBER REAL ESTATE SECURITIES, INC.; PAINEWEBBER GROUP, INC.; PAINEWEBBER INCORPORATED; and PAINEWEBBER MORTGAGE FINANCE, INC.

Respondents.

Petition For A Writ Of Certiorari To Court of Appeal For The State Of California, First Appellate District

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether it is a violation of the Due Process Clause of the Fourteenth Amendment for the amount of a punitive damages award to be evaluated according to the defendant's wealth rather than according to the reprehensibility of the defendant's conduct so that similar acts of misconduct by different defendants may result in dramatically different punitive damages awards?

LIST OF PARTIES

The names of all parties to the proceedings in the court whose judgment is sought to be reviewed here appear in the caption of the case. Petitioner, Fireman's Fund Insurance Company, is a wholly owned subsidiary of Allianz of America, Inc. Fireman's Fund Insurance Company has no non-wholly owned subsidiaries.

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PETITION FOR A WRIT OF CERTIORARI

Fireman's Fund Insurance Company, Inc. ("Fireman's Fund") petitions this Court for a writ of certiorari to review the judgment and opinion of the Court of Appeal of the State of California, First Appellate District, entered in this action on January 3, 1997.

OPINIONS BELOW

The unpublished opinion of the Court of Appeal is reproduced in the Appendix ("App.") filed herewith at App. A. On February 3, 1997 the Court of Appeal denied without opinion Fireman's Fund timely petition for rehearing. The Court of Appeal's order denying the petition for rehearing is reproduced at App. B. Thereafter, on March 26, 1997, the Supreme Court of the State of California denied without opinion Fireman's Fund timely petition for review. The California Supreme Court's order denying the petition for review is reproduced at App. C.

JURISDICTION

This petition for a writ of certiorari was filed within ninety (90) days of entry of the order dated March 26, 1997 of the Supreme Court of the State of California denying the petition for review of the Court of Appeal's opinion and judgment. This Court has jurisdiction to review the judgment of the Court of Appeal by writ of certiorari pursuant to 28 U.S.C. § 1257.

CONSTITUTIONAL PROVISIONS INVOLVED

This case presents questions under the Due Process Clause of the Fourteenth Amendment to the United States Constitution.

STATEMENT OF THE CASE

This case concerns the "[e]lementary notions of fairness enshrined in this Court's jurisprudence . . . that a person receive fair notice not only of conduct that will subject him to punishment, but also of the severity of the penalty a State may impose." *BMW of North America, Inc.* v. *Gore*, __ U.S. __; 116 S. Ct. 1589, 1598 (1996). It arises from a commercial dispute between corporations, Fireman's Fund and respondent PaineWebber.[1] The wrongdoing involved in this case was Fireman's Fund's decision not to contribute to the settlement of a suit against PaineWebber. (App. A-1.) The harm Fireman's Fund was found to have inflicted on PaineWebber consisted of purely economic damages of $3 million the jury determined Fireman's Fund should have contributed to the settlement.

The commercial dispute between Fireman's Fund and PaineWebber resulted in a $21 million punitive damages award against Fireman's Fund. (App. A-1.) The California Court of Appeal affirmed that award. In doing so, the Court of Appeal primarily relied on the rationale that "the wealthier the wrongdoer, the larger the award of punitive damages." (App. A-28.) The court therefore concluded the $21 million award was "adequate, but not excessive, to punish a company as wealthy as Fireman's Fund." (App. A-28, emphasis added.)

[1] "PaineWebber" refers collectively to respondents PaineWebber Real State Estate Securities, Inc., PaineWebber Group, Inc., PaineWebber Incorporated and PaineWebber Mortgage Finance, Inc.

Nature of the Action

This action arose from a suit brought against PaineWebber by Homestead Savings and Loan ("the Homestead suit"). PaineWebber and Homestead entered into a five-year contract which created a program for the acquisition, servicing and sale of mortgage loans insured by the Federal Housing Administration or guaranteed by the Veteran's Administration. Homestead sued PaineWebber for breach of that contract, injunctive relief, interference with prospective economic advantage and for defamation. (App. A-2, 3.)

Fireman's Fund insured PaineWebber under an excess liability policy. (App. A-1.) The parties agreed that defamation was the only claim asserted against PaineWebber that would have been covered by the Fireman's Fund policy. (App. A-4.)

In the course of the trial of the Homestead suit, PaineWebber settled the case for $20,750,000. (App. A-1.) PaineWebber demanded that Fireman's Fund contribute $3 million to this settlement. (App. A-11.) Fireman's Fund did not deny coverage for the defamation claim, but refused to consent or contribute to the settlement at that time. (App. A-11.)

PaineWebber then commenced this action against Fireman's Fund for breach of the insurance contract and breach of the implied covenant of good faith and fair dealing. PaineWebber also sought punitive damages. Fireman's Fund defended PaineWebber's suit on two principal grounds. Fireman's Fund contended that it had not breached its insurance contract by declining to contribute to the settlement of the Homestead suit. Fireman's Fund relied on the policy's terms which limited Fireman's Fund's obligation to indemnify to (a) a judgment after trial for covered damages or (b) a settlement to which Fireman's Fund had consented in writing.[2] (App. A-19.) At the time it declined to contribute to

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[2] The two policy provisions at issue are as follows:

Condition D provided that "[t]he insured shall not at any time make or authorize an admission of liability or attempt to settle or otherwise dispose of any claim or suit without the written consent of [Fireman's Fund]."

PaineWebber's settlement of the Homestead suit, California appellate decisions had upheld such provisions. *See e.g., Doser* v. *Middlesex Mutual Ins. Co.,* 101 Cal. App. 3d 883, 162 Cal. Rptr. 115 (1980); *Clark* v. *Bellefonte Ins. Co.,* 113 Cal. App. 3d 326, 169 Cal. Rptr. 832 (1980); *Finkelstein* v. *20th Century Ins. Co.,* 11 Cal. App. 4th 926, 14 Cal. Rptr. 2d 305 (1992).

With respect to PaineWebber's insurance bad faith claim, Fireman's Fund contended that even if it were found to have breached the insurance contract, its conduct was not unreasonable because there at least existed a "genuine issue" as to its obligation to contribute the settlement. Under California law, unreasonable conduct is the *sine qua non* of the tort of bad faith. *See, e.g., Opsal* v. *United Services Auto. Ass'n,* 2 Cal. App. 4th 1197, 1205, 10 Cal. Rptr. 2d 352 (1991) (the "ultimate test" of bad faith liability is not whether the withholding of benefits was right or wrong, but "whether the refusal to pay policy benefits was unreasonable"). Bad faith liability, therefore, cannot be imposed where there 'exist[s] a *genuine issue* as to [the insurer's] liability under California law." *Id.* (emphasis added).

Condition O provided that a final judgment was a precondition to Fireman's Fund's obligation to indemnify:

> [Fireman's Fund] shall be liable for payment under this policy only after the insured and the Primary Insurers have paid or become obligated to pay the applicable amount or amounts of such insurance following final judgment against the Insured after actual trial or by written agreement of the Insured, the claimant, [Fireman's Fund] and the aforesaid insurers. . . .
>
> With respect to any claim or suit to which the above does not apply, [Fireman's Fund] shall be liable for payment only after the Insured shall have fully complied with all the terms of this policy and the amount of the Insured's obligation to pay shall have been finally determined either by judgment against the Insured after actual trial or by written agreement of the Insured, the claimant and [Fireman's Fund].

(App. A-4.)

Painewebber's suit against Fireman's Fund was tried to a jury. The trial of this commercial dispute between corporations of comparable stature turned solely on Fireman's Fund's handling of a single claim—*i.e.*—its refusal to accede to PaineWebber's demand that it contribute to the settlement of the Homestead suit. The harm suffered by PaineWebber resulted in purely economic damages. PaineWebber did not present any evidence that Fireman's Fund's conduct threatened public health or safety or involved fraud or physical intimidation. Nor was there any evidence of widespread, invidious corporate practices or recidivist conduct.

The jury returned a $3 million verdict for compensatory damages which represented the amount the jury determined Fireman's Fund should have contributed to the settlement of the Homestead suit. The jury also found that Fireman's Fund acted with "malice"[3] in declining to contribute to the settlement and awarded $21 million in punitive damages. (App. A-25.)

The $21 million punitive damage award stands in stark contrast to the maximum $10,000 statutory penalty imposed by the California legislature for insurance bad faith conduct. Cal. Ins. Code § 770.035 Even the willful violation of a cease and desist order issued for insurance bad faith conduct carries a maximum statutory penalty of only $55,000. Cal. Ins. Code § 790.07.

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[3] California's punitive damages statute gives the jury discretion to award punitive damages if it is found that the defendant engaged in "oppression, fraud or malice." Cal. Civil Code § 3294 (c).

"Malice" is broadly defined in that statute as "conduct which is intended by the defendant to cause injury to the plaintiff or despicable conduct which is carried on with a willful and conscious disregard of the rights and safety of others." Cal. Civil Code § 3294 (c). *Cf. BMW,* 116 S. Ct. at 1605 (nearly identical punitive damages statute "provided no significant constraints or protection against arbitrary results") (Breyer, J., concurring).

Proceedings Below

Fireman's Fund asserted that the punitive damages award violated the Due Process Clause in its motion for new trial, which motion was denied. (App. D.) Fireman's Fund again asserted its constitutional challenge to the punitive damagse award in the Court of Appeal and in its petition for review by the California Supreme Court. (App. E, F.)

The fundamental position advanced by Fireman's Fund was that the $21 million punitive damage award cannot survive the review mandated by the Court in *BMW,* 116 S. Ct. 1589. *BMW* teaches that punitive damage awards must be tested against three "guideposts." First, *BMW* requires that "the degree of reprehensibility of the defendant's conduct" be examined; an isolated contractual dispute between two major corporations shares none of the aggravating factors the Court found significant in *BMW.* Second, the ratio of punitive damages awarded to the threatened and actual harm inflicted must be examined. Here, the threat of harm was slight while the ratio of punitive damages to the $3 million compensatory damage award (7 to 1) was high. Third, *BMW* provides that excessiveness must be judged by comparing the punitive damages award to the civil or criminal penalties that could be imposed for comparable misconduct. A comparison of the $21 million award to the $10,000 California statutory penalty for insurance bad faith compels the conclusion that the punitive damage award was excessive. Cal. Ins. Code § 790.035. Fireman's Fund advanced the further proposition that its wealth was not an appropriate consideration in light of this Court's analysis in *BMW.* (App. E, F.)

The Court of Appeal affirmed the $21 million punitive damage award without reference to this Court's instructions in *BMW,* 116 S. Ct. 1589. Instead, the court gave great weight to the jury's verdict and looked to the three factors specified by California law for evaluating the excessiveness of punitive damages: "'The nature of the defendant's acts, the amount of compensatory damages awarded and the wealth of the

defendant.'" (App. A-27, citing *Devlin* v. *Kearny Mesa AMC/Jeep/Renault, Inc.*, 155 Cal. App. 3d 381, 388, 202 Cal. Rptr. 204 (1984)).

The court's entire analysis of the excessiveness of the $21 million punitive damage award was as follows:

> Because the purposes of punitive damages are to punish the wrongdoer and to make an example of him, *the wealthier the wrongdoer, the larger the award of punitive damages.* [Citation omitted.] "Net worth generally is considered the best measure of a defendant's 'wealth' for purposes of assessing punitive damages." [Citation omitted.] There is no fixed ratio to determine the proper proportion between punitive and compensatory damages. [Citations]" Ratios of 2000:1, 74:1, 25.6:1 and 17:1 have been upheld.
>
> All of the above factors support the award in the present case. The cavalier manner in which Fireman's Fund treated its insured regarding the "high potential" Homestead case was reprehensible. Large corporations such as PaineWebber have the same right to be treated fairly as do insureds of less means. A ratio of 7:1 between compensatory and punitive damages is well within acceptable limits. Damages of $21 million are *adequate, but not excessive to punish a company as wealthy as Fireman's Fund.*

(App. A-27-28.) (emphasis added).

REASONS FOR GRANTING THE WRIT

The question presented by this petition is not simply whether the lower court erred in affirming the $21 million punitive damage award against Fireman's Fund. Rather, this

petition presents a question of broader constitutional dimension: whether a punitive damage award that is tantamount to a severe criminal penalty can be justified solely by the defendant's wealth. The lower court's affirmance of the $21 million punitive damages award in this case rested on the premise that "the wealthier the wrongdoer, *the larger the award of punitive damages.*" (App. A-28.) Fireman's Fund submits that making the defendant's wealth the determinant of the appropriate amount of punitive damages is constitutionally infirm. By that measure, two wrongdoers can engage in identical misconduct causing identical harm and yet be subjected to radically different penalties. In that circumstance, neither person has "fair notice" of the severity of the penalty the State may impose for a class of conduct.

The protection from grossly excessive punitive damages and the right to fair notice afforded by the Due Process Clause should not vary according to the wealth of the defendant. To the contrary, the purpose of the Due Process Clause is "to assure the uniform general treatment of similarly situated persons that is the essence of law itself." *BMW,* 116 S. Ct. at 1605 (Breyer, J., concurring). The Court should issue a writ of certiorari.

I. ASSESSING PUNITIVE DAMAGES ON THE BASIS OF THE DEFENDANT'S WEALTH VIOLATES DUE PROCESS

Defining the constitutional limits of punitive damages involves balancing a person's due process rights with a State's legitimate interests. The Court has long-recognized that punitive damages are a quasi-criminal sanction which may be imposed to further a State's interests in punishing unlawful conduct and deterring its repetition. *See, e.g., Gertz* v. *Robert Welch, Inc.,* 418 U.S. 323, 350 (1974). The Court has also found that when a punitive damage award is "grossly excessive" in relation to the State's interests, the award amounts to an "arbitrary deprivation of property without due process of law." *TXO Production Corp.* v. *Alliance Resources Corp.,*

509 U.S. 443, 454 (1993) (plurality opinion). Moreover, "[e]lementary notions of fairness enshrined in this Court's jurisprudence dictate that a person receive fair notice not only of conduct that will subject him to punishment, but also of the severity of the penalty a State may impose." *BMW*, 116 S. Ct. at 1598.

In *BMW* the Court achieved the balance that allows a State to further its interest in punishment and deterrence, while at the same time protecting a person's due process rights to be free from constitutionally arbitrary awards and to have fair notice of the magnitude of the sanction a State might impose. The Court set forth three "guideposts" by which punitive damage awards are to be measured. Id. at 1598. To ensure due process, punitive damages awards must (1) bear a reasonable relationship to the "degree of reprehensibility of the defendant's conduct;" (2) have a "reasonable relationship" to the "actual harm inflicted" as measured by the compensatory damages awarded; and (3) the civil and criminal penalties that could be imposed for comparable misconduct must indicate the severity of punishment that might be imposed by a punitive damage award. *Id.* at 1598-1599.

The wealth of the defendant is not among the "guideposts" laid down in *BMW*. To be sure, the Court's omission of the defendant's wealth from the constitutional standard does not, by itself, mean that consideration of that wealth is wholly irrelevant in the assessment of punitive damages. Application of the *BMW* guideposts to the punitive damages award in this case, however, demonstrates that the standard employed by the lower court—"the wealthier the wrongdoer, the larger the award of punitive damages"—eviscerates the constitutional safeguards given effect in *BMW*.

A. Multimillion Punitive Damage Awards Cannot Be Constitutionally Justified By The Defendant's Wealth

The fundamental infirmity in making punitive damages a function of the defendant's wealth, as the court did below, is that it does not properly serve a State's legitimate interests in punishing wrongdoers and deterring misconduct, but does

invite "grossly excessive" punitive damage awards. Indeed, Justice Breyer recognized this in his concurring opinion in *BMW.* In *BMW,* 116 S. Ct. 1589, as here, the Court had before it a state law punitive damages standard which included consideration of the "financial position of the defendant." *Id.* at 1606. Justice Breyer concluded that this factor—*i.e.,* the defendant's wealth—did "not act as a significant constraint on punitive damage awards. Rather, it provides an open-ended basis for inflating awards when the defendant is wealthy. . . ." *Id.* at 1607. Justice Breyer further explained that while this circumstance does not render the use of the defendant's wealth "unlawful or inappropriate; it . . . cannot make up for *the failure of other factors, such as 'reprehensibility,'* to constrain significantly an award that purports to punish a defendant's conduct." *Id.* (emphasis added). In *Pulla* v. *Amoco Oil Co.,* 72 F.3d 648 (8th Cir. 1995), former Justice White presaged the analysis set forth in the *BMW* concurring opinion: "[w]hile a defendant's wealth may be taken into account in order to ensure that an award will adequately deter any future misconduct, a defendant's wealth cannot alone justify a large punitive damage award." *Id.* at 659 n. 16.

This Court echoed both Justice Breyer and former Justice White in its majority opinion. The Court found itself unable to "accept the conclusion of the Alabama Supreme Court that BMW's conduct was sufficiently egregious to justify a punitive sanction that is tantamount to a severe criminal penalty." *BMW,* 116 S. Ct at 1604. The Court further concluded that the multimillion dollar award at issue could not be justified by virtue of BMW's status. As the Court explained, "[t]he fact that BMW is a large corporation rather than an impecunious individual does not diminish its entitlement to fair notice of the demands that the several States impose on the conduct of its business." *Id.*

The Court also rejected the argument that large punitive damages were appropriate because it "prompted a change in [BMW's] policy." *Id.* at 1603. Implicit in that argument was the notion that BMW, as a large corporation, needed a large

award in order to effectuate the State's legitimate interest in deterring its misconduct. Although BMW did change its corporate policy, this Court made clear that fact "sheds no light on the question whether a lesser deterrent would have adequately protected" the State's interest in deterrence. *Id.* What matters is effective deterrence, not merely the financial condition of the defendant. The question is whether "a more modest sanction would not have been sufficient. . . ." *Id. See also Continental Trend Resources, Inc.* v. *OXY, USA, Inc.*, 101 F.3d 634, 641 (10th Cir. 1996) (*BMW* "downplayed the defendant's wealth as a justification for increasing punitive damages" and focused on "the minimum level of penalty necessary to achieve the state's goal of deterrence")

The principle that emerges from these opinions is that a punitive damage award that fails to meet the guideposts set forth in *BMW* cannot be rescued from constitutional infirmity merely because the defendant is wealthy. Rather, the proclivity to rationalize substantial punitive damage awards as being necessary to effectively punish and deter wealthy defendants must yield to the constitutional limit discerned by applying the objective factors of degree of reprehensibility, reasonableness of the relationship of punitive damages to actual harm and sanctions for comparable conduct. *See also Florez* v. *Delbovo*, 939 F. Supp. 1341, 1349 (N.D. Ill. 1996) ("wealth cannot save a punishment that is deemed to be excessive under the *BMW* approach").

B. The $21 Million Punitive Damage Award Does Not Meet The *BMW* Objective Factors And Therefore Violates Due Process Because It Is Founded On The Defendant's Wealth

This case dramatically illustrates why direction from this Court is needed. When measured against the guideposts dictated by the Court in *BMW*, it is apparent that Fireman's Fund's wealth, not its conduct, was the determinant of the $21 million punitive damages award. Indeed, the lower court rationalized that the $21 million award was justified by Fireman's Fund wealth. The fundamental problem is not simply

that the punishment exacted of Fireman's Fund was more than it should have been. The deeper flaw is that making wealth the determining factor in testing the excessiveness of any punitive damages award deprives one of fair notice of the severity of the penalty a State might impose for a class of conduct.

The essential teaching of *BMW* is that fair notice is derived from awareness that engaging in a class of misconduct can result in a penalty within a reasonably definable range. Thus, when the range of punishment becomes a function of the wrongdoer's financial status, rather than conduct, fair notice evaporates. This is because defendants guilty of similar misconduct — indeed, identical misconduct — become subject to wholly different punishments.

When the award in this case is tested against the *BMW* guideposts, it is evident that Fireman's Fund was deprived of fair notice that its conduct would subject it to an award that is "tantamount to a severe criminal penalty." *BMW,* 116 S. Ct. at 1604.

1. Degree of Reprehensibility

"Perhaps the most important indicium of the reasonableness of a punitive damages award is the degree of reprehensibility of the defendant's conduct." *Id.* at 1599. This principal reflects the view that "some wrongs are more blameworthy than others." *Id.* Simply because "conduct is sufficiently reprehensible to give rise to tort liability, and even a modest award of exemplary damages, does not establish the high degree of culpability that warrants a substantial punitive damages award." *Id.,* at 1601. Thus, in determining if a substantial punitive award transgresses constitutional limits, the critical inquiry is whether the conduct at issue is so culpable that the award exacts an appropriate punishment in furtherance of the State's legitimate interests. In *BMW,* 116 S. Ct. 1589, the Court identified the "aggravating factors associated with particularly reprehensible conduct" that justify a severe sanction: (1) whether "a defendant has repeatedly engaged in prohibited conduct while knowing or suspecting that it was unlawful"; (2) whether the harm

caused was to the health or safety of individuals or instead purely economic harm; and (3) whether the "target" is "financially vulnerable." *Id.* at 1599.

None of these "aggravating factors" is present here. This is a case of an isolated dispute involving a single insurance claim by PaineWebber. The only harm caused by Fireman's Fund's conduct was economic, *i.e.,* the costs of the settlement contribution that Fireman's Fund was obligated to pay. Nor was the "target" "financially vulnerable." To the contrary, PaineWebber is a large, sophisticated corporation "with the financial resources to weather . . . sharp business practices." *Las Palmas Associates* v. *Las Palmas Center Associates,* 235 Cal. App. 3d 1220, 1255, 1 Cal. Rptr. 2d 301 (1991).

The lower court does make the conclusionary statement that Fireman's Fund's conduct was "egregious" because "it completely disregarded the long-established law." (App. A-26.) The lower court's opinion belies that statement. Fireman's Fund's conduct was founded on a good faith belief that it had a contractual right to do precisely what it did. It at arrived at that belief from California case law that existed at the time it declined to contribute to PaineWebber's settlement of the Homestead suit in 1987. As explained above, at page 4, in *Doser,* 101 Cal. App. 3d 883, 162 Cal. Rptr. 115, the court upheld the insurance contract provisions on which Fireman's Fund relied. Doser was decided in 1980.[4]

Despite stating that it disregarded "long-established law," the lower court did not find Fireman's Fund had wrongfully relied on the law as it existed when Fireman's Fund declined to contribute to the Homestead settlement. Rather, the court found more persuasive the reasoning of two decisions rendered years later: *Camelot by the Bay Condominium Owner's Ass'n* v. *Scottsdale Ins. Co.,* 27 Cal. App. 4th 33, 32 Cal. Rptr. 2d 354 (1994) and *Diamond Heights Homeowners Ass'n* v. *National American Ins. Co.,* 227 Cal. App. 3d 563,

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[4] *Doser* was subsequently reaffirmed by *Finkelstein,* 11 Cal. App. 4th 926, 14 Cal. Rptr. 2d 305.

227 Cal. Rptr. 906 (1991). (App. A-22.) An erroneous but not unreasonable interpretation of its contractual rights premised on existing case law cannot constitute sufficiently reprehensible conduct to justify a $21 million punitive damage award. To the contrary, given the state of the law at the time Fireman's Fund acted, it "could reasonably interpret [those cases] as establishing safe harbors" of acceptable insurer conduct. *BMW,* 116 S. Ct. at 1600.

2. Relationship of Compensatory Damages to Punitive Damages

This Court also endorsed the proposition that "a comparison between the compensatory award and the punitive award is significant." *Id.* at 1602. The Court acknowledged that:

> low awards of compensatory damages may properly support a higher ratio, if, for example, a particularly egregious act has resulted in only a small amount of economic damages. A higher ratio may also be justified in cases in which the injury is hard to detect or the monetary values of noneconomic harm mights have been difficult to determine.

Id.

The Court, however, rejected the "categorical approach" of drawing "a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable. . . ." *Id.* The "proper inquiry" is " 'whether there is a reasonable relationship between the punitive damages award and the harm likely to result from the defendant's conduct as well as the harm that actually has occurred.' " *Id.* (*quoting TXO Production Corp.* v. *Alliance Resources Corp.,* 509 U.S. 443, 460 (1993) (quotation marks, citation and emphasis omitted)).

Expressed in terms of a simple ratio, the relationship between the $3 million compensatory damages and the $21 million in punitive damages awarded in this case is 7 to 1. That ratio might be appropriate if Fireman's Fund's misconduct had resulted in nominal injury to a large number of

people or if the injury Fireman's Fund caused was difficult to determine. Neither of those circumstances exist. Fireman's Fund harmed no one but PaineWebber and that harm (the amount Fireman's Fund's should have contributed to the settlement) was easily determined.

A 7 to 1 ratio does not reflect a "reasonable relationship" of the punitive damages to the harm done to PaineWebber by Fireman's Fund's handling of a single claim. Indeed, in *Pacific Mutual Life Ins. Co.* v. *Haslip,* 499 U.S. 1 (1991), the Court noted that a ratio of "4 to 1" in a case involving economic injury was "close to the line" of constitutional impropriety. *Id.* at 23-24.[5]

3. Sanctions for Comparable Misconduct

BMW's fair notice requirement makes it essential to compare punitive damage awards with "the civil or criminal penalties that could be imposed for comparable misconduct." *Id.* The statutory penalties a State imposes for comparable misconduct is significant for two reasons. First, such sanctions provide notice of the magnitude of the punitive damages a State may impose. Accordingly, when punitive damages actually awarded are substantially greater than the established statutory fines, a defendant has not received the *fair* notice mandated by the Due Process Clause. Thus, in *BMW,* 116 S. Ct. 1589, the Court concluded that a maximum statutory penalty of $10,000 for the relevant misconduct did not provide BMW with fair notice that it could be subject to the $2 million punitive damages awarded. *Id.* at 1603. The same holds true here. California's maximum statutory penalty for insurance bad faith is $10,000. Cal. Ins. Code § 790.035. Willful violation of a cease and desist order risks a maximum penalty of only $55,000. Cal. Ins. Code § 790.07. These fines cannot be said to give fair notice of the potential imposition

[5] In *BMW,* the Court suggested in affirming the punitive damages award in *TXO Production Corp.* v. *Alliance Resources Corp.,* 509 U.S. 443 (1993), the relevant ratio was 10 to 1. *BMW* 116 S. Ct. at 1602. The conduct at issue in *TXO,* however, was a "continuing pattern and practice of fraud, trickery and deceit" and thus involved a far higher degree of reprehensibility than Fireman's Fund's conduct.

of a $21 million punitive damages award, a sum which is more than 380 times the maximum statutory penalty.

Statutory penalties are also significant to the constitutional punitive damages equation given the Court's acknowledgement that a State is entitled to determine what sanctions are necessary to effectuate its legitimate interests in punishment and deterrence. Thus, "a reviewing court engaged in determining whether an award of punitive damages is excessive should 'accord "substantial deference" to legislative judgments concerning appropriate sanctions for the conduct at issue.' " *Id.* (*quoting Browning-Ferris Industries of Vt., Inc.* v. *Keloc Disposal, Inc.*, 492 U.S. 257, 301 (1989) (O'Connor, J., concurring and dissenting) (quotation marks and citation omitted)). The California legislature has evidently concluded that a million dollar award is unnecessary to deter even intentional bad faith conduct, much less a $21 million award.

In sum, the $21 million punitive damage award imposed here cannot be justified by the guideposts this Court established to ensure that punitive damages awards pass constitutional muster. Rather, the magnitude of the sanction is a function of the lower court's reliance on the maxim that "the wealthier the wrongdoer, the larger the award of punitive damages."

This case thus makes manifest that measuring the propriety of punitive damages on the basis of the defendant's wealth "provides an open-ended basis for inflating awards. . . ." *BMW,* 116 S. Ct at 1607, (Breyer, J., concurring). It exemplifies the entrenched adherence to a standard which makes the defendant's wealth the basic unit used in meting out punishment, rather than the harm (actual or threatened) done to the plaintiff. It epitomizes the failure of this approach to achieve the appropriate balance between a State's legitimate interests in punishment and deterrence and a person's right to both fair notice of the severity of the penalty a State might impose and protection from punitive awards that are in the zone of constitutional arbitrariness. Admittedly, a State has a legitimate interest in punishing wrongdoers. But

it can have no legitimate interest in perpetuating a punitive system that exacts punishment based on wealth.

CONCLUSION

For the foregoing reasons, a writ of certiorari should issue to review the decision of the California Court of Appeal.

Respectfully submitted,

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NOT TO BE PUBLISHED IN OFFICIAL REPORTS

In The Court Of Appeal
OF THE
State Of California

FIRST APPELLATE DISTRICT
DIVISION THREE

PAINEWEBBER REAL ESTATE SECURITIES, INC., et al.,
Plaintiffs and Respondents,

v.

FIREMAN'S FUND INSURANCE COMPANY, INC.,
Defendant and Appellant.

A063060

(City and County of San Francisco Super. Ct. No. 888592)

FILED
Court of Appeal-First App. Dist.
JAN 3 1997
RON D. BARROW, CLERK
By_____
DEPUTY

At all material times, plaintiffs and respondents PaineWebber Real Estate Securities, Inc., PaineWebber Group, Inc., PaineWebber Incorporated, and PaineWebber Mortgage Finance, Inc. (PaineWebber) were insured by a "supercover umbrella and excess liability" insurance policy issued by defendant and appellant Fireman's Fund Insurance Company, Inc. (Fireman's Fund), which covered damages from over $1,000,000 up to $25,000,000 for defamation of a business, but not for breach of contract. The instant appeal arose out of the refusal of Fireman's Fund to contribute funds to the settlement of a federal lawsuit between PaineWebber and Homestead Savings & Loan (Homestead), wherein PaineWebber agreed to pay $20,750,000 to Homestead.

APPENDIX A

In a three-stage trial, a jury awarded PaineWebber compensatory damages of $3,000,000 and punitive damages of $21,000,000 on the basis of contract and tort causes of action for breach of the implied covenant of good faith and fair dealing and for breach of statutory duties. After a court trial, the court awarded PaineWebber attorney fees of $1,511,444.46 and costs of $307,675.47, for a total of $1,819,119.93. Prejudgment interest of $2,840,393.32 was also awarded. The total judgment against Fireman's Fund was for $28,659,513.25.

Fireman's Fund contends that it properly refused to contribute to the settlement of *Homestead* v. *Paine Webber (Homestead* case) on the ground that the potential damages which formed the basis of the settlement were not covered by the excess policy. It also challenges the jury instructions, verdict of liability and awards of damages on legal and factual grounds. We affirm.

FACTUAL AND PROCEDURAL BACKGROUND

On June 15, 1983, Homestead and PaineWebber entered into a five-year contract which created a program for the acquisition, servicing and sale of mortgage loans insured by the Federal Housing Administration (FHA) or guaranteed by the Veteran's Administration (VA). PaineWebber agreed to refer sellers/originators of the government loans to Homestead and Homestead agreed to purchase the loans. Servicing fees would be collected by Homestead and the loans were arranged into Government National Mortgage Association (GNMA) securities, which Homestead sold to PaineWebber. In the contract, PaineWebber "agreed to use its best efforts" to refer government loans in the following amounts: $400 million from June 15, 1983, through June 15, 1984; $800 million from June 15, 1984, through June 15, 1985; $1.2 billion from June 15, 1985, through June 15, 1986; $1.2 billion from June 15, 1986, through June 15, 1987; and $1.4 billion from June 15, 1987, through June 15, 1988.

On September 12, 1985, Homestead filed a complaint against PaineWebber in the United States District Court for the Northern District of California, which alleged six causes of action. The first three alleged that PaineWebber had breached several provisions of the 1983 contract, while the sixth sought injunctive relief.

The fourth cause of action alleged "[t]ortious [i]nterference with [p]rospective [e]conomic [a]dvantage" as follows: PaineWebber falsely stated to the sellers of loans that "[Homestead] was not in the business of purchasing of [m]ortgage [l]oans and their servicing rights and that [PaineWebber] had no agreement with [Homestead] regarding the purchase of said [m]ortgage [l]oans and their servicing rights." These remarks directly and proximately caused Homestead to lose "in excess of $1,000,000" of "business with a large number of prior and prospective sellers of [m]ortgage [l]oans."

The fifth cause of action alleged damages "in excess of $1,000,000" for "[s]lander, [d]isparagement and [t]rade [l]ibel" based on false statements by PaineWebber commencing "sometime in 1985" "about Homestead, its business plan, services and its interest in remaining a purchaser of [m]ortgage [l]oan servicing rights." Punitive damages were sought in the fourth and fifth causes of action.

PaineWebber filed an answer, amended answer and counterclaim to the Homestead complaint. Its principal defenses in the *Homestead* case were: (1) PaineWebber did not tell sellers/originators of home loans that Homestead was out of the market for government loans; (2) any such statements were true because Homestead lost the loan servicing business by lowering the price paid for VA loans and due to problems servicing loans; (3) federal regulators would have removed Homestead from the government loan market; and (4) damages were speculative, the loan program was unprofitable and Homestead should have mitigated damages.

The *Homestead* case was assigned to Chief District Court Judge Robert F. Peekham. Homestead was represented by

Brobeck, Phleger & Harrison, principally by Franklin Brockway Gowdy. PaineWebber was represented by Keesal, Young & Logan, principally by Samuel A. Keesal, Jr. and Peter R. Boutin. Judge Peckham and each of the involved attorneys had excellent reputations.

In pretrial statements, settlement conference statements, trial briefs, memorandum and oral argument to Judge Peckham, Homestead's attorneys always vigorously pursued its fourth and fifth causes of action (collectively, the defamation causes of action). PaineWebber's attorneys consistently maintained their defenses with equal force. The Keesal firm always believed that defamation was an important part of the case. Breach of contract was also fully argued by the attorneys. In fact, the Keesal firm considered that the breach of contract and defamation were inextricably intertwined and the damages for each were identical. The Keesal firm believed in their defenses, but as Boutin acknowledged, he was an advocate for his client.

PaineWebber was insured by a "supercover umbrella and excess liability policy" issued by Fireman's Fund. On appeal it is undisputed that at all material times the Fireman's Fund policy covered liability incurred by PaineWebber, between the amounts of $1 million and $25 million, arising out of the defamation causes of action, but not for breach of contract or punitive damages.

Condition D of the policy states in pertinent part: "The [i]nsured shall not at any time make or authorize an admission of liability or attempt to settle or otherwise dispose of any claim or suit without the written consent of [Fireman's Fund]." Condition H states in pertinent part: "when insurance is available to the [i]nsured under any [p]rimary [i]nsurance, . . . [Fireman's Fund], although without obligation to do so, shall have the right and opportunity to associate with the [p]rimary [i]nsurer in the defense and control of any claim or suit reasonably likely to involve [Fireman's Fund] under this policy."

Condition O states in pertinent part: "[Fireman's Fund] shall be liable for payment under this policy only after the [i]nsured and the [p]rimary [i]nsurers have paid or become obligated to pay the applicable amount or amounts of such insurance following final judgment against the [i]nsured after actual trial or by written agreement of the [i]nsured, the claimant, [Fireman's Fund] and the aforesaid insurers. . . . [¶] With respect to any claim or suit to which the above does not apply, [Fireman's Fund] shall be liable for payment under this policy only after the [i]nsured shall have fully complied with all the terms of this policy and the amount of the [i]nsured's obligation to pay shall have been finally determined either by judgment against the [i]nsured after actual trial or by written agreement of the [i]nsured, the claimant and [Fireman's Fund]."

A financial institutions limitation and exclusions clause stated in pertinent part that the policy did not apply to "liability arising out of any negligent act, error or omission in the performance of professional services for others by or on behalf of the [i]nsured. . . ."

The primary policy underlying the Fireman's Fund excess policy was issued by National Union Insurance Company. It covered the same liabilities and period of time as the Fireman's Fund excess policy, for up to $1 million. Other policies, including a $1 million primary policy by Centennial Insurance Company, covered the same liabilities for different periods of time.

On July 30, 1986, PaineWebber informed its insurance broker of the *Homestead* case, which alleged that PaineWebber failed to comply with a contract "and slandered and libeled Homestead's business." A copy of the complaint was enclosed. The broker was requested to notify the primary insurance companies and to obtain their approval to retain Keesal, Young & Logan to represent PaineWebber.

On August 5, 1986, the primary insurance companies were notified. On August 11, 1986, the broker sent "a complete

copy of [its] file" to the San Francisco office of Fireman's Fund. In August 1986, litigation specialist Ralph Woodard was assigned the case by Fireman's Fund and acknowledged receipt of the file. Also, in August 1986, senior liability adjuster Ramona Eiseman was assigned the case by Centennial. National Union assigned the case to a litigation specialist. On December 6, 1986, Eiseman left Centennial and claims manager Karen Plastiras was assigned to the case. Eiseman obtained employment as a litigation supervisor for National Union and the *Homestead* case was transferred to her. Plastiras classified Eiseman as "a very competent claims handler."

National Union and Centennial retained counsel for the *Homestead* case, but Eiseman and Plastiras attended meetings with the Keesal firm and fully participated in the decision-making process involving their companies' policies toward the *Homestead* case.

On August 26, 1986, Woodard wrote out his "initial suit review." He observed that Fireman's Fund was an excess carrier as to "slander [and] trade libel allegations." Woodard attempted to gather data about the *Homestead* case. His first priorities were to obtain copies of the Fireman's Fund excess policy and to contact the primary carriers.

On October 1, 1986, Boutin mailed an insurance policy to Woodard which turned out to be the wrong policy. The accompanying letter advised Woodard of current developments in the *Homestead* case and stated that Woodard should not hesitate to ask for further information. On October 8, 1986, the correct policy was mailed. At all material times thereafter, the Keesal firm provided the designated representatives of Fireman's Fund and the other carriers with all the relevant transcripts, briefs, memoranda and other documents from the *Homestead* case. Eventually "tons of paper" were transmitted. Keesal and/or Boutin also constantly reported to Fireman's Fund and the other carriers about the progress of the case and their appraisal of the probable outcome.

Woodard was in charge of the *Homestead* case for Fireman's Fund until March 10, 1987. He believed that Fireman's Fund might be liable for PaineWebber's alleged statements that Homestead was not in the loan business and did not have an agreement with PaineWebber. Notes prepared by Woodard in October 2, 1986, observe that the primary carriers were providing a defense to PaineWebber and that Fireman's Fund "should monitor." Throughout the time that Woodard was in charge of the case he played an active role in the investigation and sought to keep in communication with the primary carriers. Woodard had at least one telephone conversation with a representative of a primary carrier.

Also on October 1, 1986, Centennial sent a reservation of rights letter to Boutin, which acknowledged that the defamation causes of action of the Homestead complaint "create[d] a potential claim of insurance coverage." The letter further stated that no coverage existed for the breach of contract causes of action or for defamation outside the period of time covered by the policy. Centennial agreed to pay the legal costs of the Keesal firm as independent counsel for PaineWebber, pursuant to *San Diego Federal Credit Union* v. *Cumis Ins. Society, Inc.* (1984) 162 Cal.App.3d 358. National Union also agreed to such arrangement.

An investigation report of Woodard, dated February 13, 1987, states that Homestead sought damages of $366 million for the defamation causes of action and would not settle for less than $300 million. Further, "[t]he question here reduces to whether, in fact, the statements, although disparaging, were, in fact, *truth.*" (Original emphasis by Woodard.) On the same date Fireman's Fund, through Woodard, sent Boutin a reservation of rights letter which accepted coverage for "an award or judgment" on the defamation causes of action, but otherwise denied coverage. On February 24, 1987, National Union sent a reservation of rights letter which affirmed that the defamation causes of action "create[d] a potential claim of insurance coverage." On April 20, 1987, Fireman's Fund sent a supplementary reservation of rights

letter asserting that the financial institutions exclusion in the excess liability policy exempted it from coverage. Fireman's Fund did not subsequently place strong reliance on the financial institutions exclusion.

On March 10, 1987, Woodard transferred the *Homestead* case to director of excess claims Kenneth Beck at the home office of Fireman's Fund in Novato, California. Beck became the "point person" for Fireman's Fund. In March 1987, Beck retained the law firm of Fisher & Hurst "to advise Fireman's Fund on coverage with respect to the *Homestead* case." Robert Schiff and Dennis Gildea were the principal attorneys from the Fisher firm who worked on the case. The firm and those individuals had excellent reputations.

After Beck retained the Fisher firm, he chose not to play an active role in the decision-making process involving Fireman's Fund policies toward the *Homestead* case. Beck did not: personally monitor the case, read most documents, attend meetings, or contact the primary carriers. Woodard had little to do with the case after it was transferred. The Fireman's Fund manual and printed "excess handling guidelines" mandated that the company representative should personally investigate questions of coverage, monitor a case and maintain contact with the primary carriers. Beck was aware of these requirements but he left the *Homestead* case to be resolved by the Fisher and Keesal law firms. Fireman's Fund did not raise the defense of reliance on counsel. Based on a memorandum from Beck, his superiors at Fireman's Fund evaluated the Homestead case as a "high potential claim" and were critical of the delay in transmitting it to the home office.

In a series of approximately 12 letters commencing on January 29, 1987, and continuing until the *Homestead* case was settled by PaineWebber for $20,750,000 on June 30, 1987, and at meetings on March 26, 1987, April 28, 1987, May 19, 1987, late May 1987 and June 12, 1987, the Keesal firm delivered an increasingly pessimistic message to Fireman's Fund and the primary carriers. The message was that

the trial was consistently going badly for PaineWebber. Fireman's Fund was kept up to date on the progressively mounting probability that damages for lost profits of between $85 and $158 million, as calculated by Homestead's damages expert Coopers & Lybrand, would very likely be assessed against PaineWebber on the defamation and contract causes of action. Fireman's Fund was also advised of the several attempts at settlement. The Fisher firm had an associate attend portions of the trial. No member of the Fisher firm expressed disagreement with the Keesal firm's assessment of the trial.

It was mutually agreed by PaineWebber and the insurance companies that the latter would not attend settlement conferences, since their presence might lead to even higher demands by Homestead.

A principle reason for the gloomy evaluation by PaineWebber's attorneys was the testimony of six independent third party witnesses, who were the originators/sellers of loans to Homestead under the Homestead-PaineWebber program. They testified between March 12, 1987, and April 7, 1987. Extreme satisfaction with Homestead was expressed by the witnesses, along with a desire to continue in the program. No significant problems were encountered with the servicing by Homestead. The price paid by Homestead was satisfactory even after it had been lowered for VA loans. Moreover, the vast majority of loans sold by the originators were FHA loans where the price remained constant.

The only reason these six originators/sellers ceased doing business with Homestead was that in the spring of 1985, PaineWebber employees Cosmo Fontana, John Malis, or Joyce DeRosa made one or more of the following statements to each originator: Homestead "had pulled out of the market and were no longer buying"; " 'they are no longer taking loans, period' "; "there is no more program. We don't have a source with Homestead any longer"; and Homestead was "in trouble" with the federal government "on their documents." Since the originators operated through

PaineWebber, they immediately sold their loans to other institutions. Homestead confirmed to one originator that it was out of the government loan business; another was unable to contact Homestead directly. No new loans were acquired by Homestead from its program with PaineWebber after April 12, 1985.

On February 26, 1987, another independent third party witness involved in the purchase of individual government backed loans testified that he was told by a representative of PaineWebber that the Homestead program "wasn't viable or wasn't operating, or just wasn't there." On April 9, 1987, an employee of Homestead testified that from March to the summer of 1985, she received about five or six telephone calls per week from sellers asking if Homestead was still in the market for buying government loans. The employee told the sellers to contact PaineWebber. A seller/originator who testified reported that PaineWebber stated that Homestead was no longer in the market.

Homestead had planned to call an additional ten originators, who PaineWebber's attorneys had reason to believe would give testimony similar to the six who did testify. A total of $43,028,511 in loans was sold by the six witnesses to Homestead. Another $55,704,201 was sold by the additional ten prospective witnesses. Judge Peckham had indicated that he was not interested in hearing from many more originators. Based on the originator testimony and deposition evidence, PaineWebber's attorneys came to believe that Cosmo Fontana and other PaineWebber employees could not credibly deny making the statements attributed to them.

Evidence was introduced that the federal government had imposed a supervisory agreement on Homestead which precluded it from acquiring additional loans. The federal government acted because of the problems Homestead experienced in servicing loans. However, the ranking federal government official involved with the supervisory agreement testified that it only applied to "bulk" loan acquisitions

which created unique problems and were totally different from the "spot" loan purchases which were the subject of the *Homestead* case.

Homestead's damages experts, Coopers & Lybrand, testified that Homestead suffered damages from lost profits of between $85 million and $158 million. PaineWebber's damages expert testified that Homestead actually gained $6 to $8 million by not being able to purchase additional loans, because it was losing money on the servicing.

As of May 5, 1987, Judge Peckham had made several rulings and statements which indicated he was being persuaded by Homestead's evidence. By excluding newspaper articles besmirching Homestead's business reputation, he accepted Homestead's theory that the defamation was the statements that it was out of business. The judge made reference to PaineWebber's breach of contract. He stated that "it's quite possible" the federal supervisory agreement only aimed at bulk loan acquisitions and "it can be argued that [the defense of poor servicing] lacks support in the evidence." No further testimony about Homestead's problems with servicing was seen to be necessary. A request for damages testimony, before the case on liability was completed, at minimum implied that the judge believed liability was established. On May 19, 1987, Judge Peckham stated that damages were not too speculative to be proven.

Letters and meetings specifically directed to Fireman's Fund contributing or approving the actual settlement of the *Homestead* case are as follows: PaineWebber's first request to Fireman's Fund for money to settle the *Homestead* case was in a telephone conversation and letter from Keesal to Gildea on May 13, 1987. A "formal demand" was made for $3 million. At the same time $1 million was "formally demanded" from each of the primary carriers, National Union and Centennial. Keesal's letter to Gildea states that "if the trial were to conclude today, the [c]ourt would rule against PaineWebber on all claims, including Homestead's disparagement and related claims. . . . [T]he most likely damage award would be approximately $85 million." In answer to

Gildea's objections that the damages "were not caused solely by covered risks," Keesal explained that: "Under California law, however, there is coverage where the covered risk is a concurrent proximate cause of the loss."

Also on May 13, 1987, Gildea wrote to Keesal rejecting the demand because "we see no evidence of damages caused by covered defamation in excess of the limits of available primary insurance." In addition, Gildea called Keesal's "attention to the policy provisions prohibiting the insured from settling the case without [Fireman's Fund's] consent. (See Conditions D and O of the . . . policy.) . . . Fireman's Fund does not consent to the settlement at this time. Any settlement entered by PaineWebber would be for the insured's own account."

On May 14, 1987, Eiseman wrote to her New Jersey office recommending that National Union "provide our insured with the policy limits in an attempt to expedite settlement of this matter." She reports having consulted with Gildea and lists the reasons he gave for not contributing to a settlement. Eiseman testified that her recommendation was based on her evaluation of the *Homestead* case. She "agreed completely" with the pessimistic assessment by the Keesal firm, and that breach of contract and defamation could not be separated in the *Homestead* case. The high defense costs being borne by National Union, and a desire to secure a reasonable settlement for her insured in the face of "incredible exposure" over $1 million, also entered into the decision. No one from Fireman's Fund consulted with National Union before refusing to contribute.

On May 15, 1987, Gildea wrote to Keesal reaffirming that Fireman's Fund would not contribute to or authorize a settlement and its reliance on Conditions D and O of the policy. The letter also stated: "Our view is that the claimed damages are not caused by defamation at all. No 'concurrent cause' analysis is necessary. [¶] In our phone conversation, you mentioned the possibility that the court would find damages of $85 million resulting from disparagement. You

should be advised that Fireman's Fund would not be bound by the court's allocation of damages."

In a letter of May 18, 1987, Boutin asked Gildea to reconsider his position. Boutin mentions the originator witnesses and "substantial probability" of a judgment for Homestead on the defamation causes of action for over $85 million. Gildea reasserted his refusal in a letter of May 19, 1987. He agreed that the originator witnesses "supported the disparagement claim," but insisted that the resulting potential damages were only "in the thousands." Gildea claims that Keesal "confirmed that the witnesses have not substantiated defamation damages in excess of the primary limits." Keesal strongly denied making such concession.

On May 19, and possibly again in late May 1987, Boutin and Keesal met with Gildea and Schiff. The former orally presented their evaluation of the *Homestead* case and reasons why Fireman's Fund should contribute to a settlement. Gildea and Schiff agreed with the case evaluation, except that they appraised the defamation damages to be in the range of $600,000. No explanation of the calculation was given.

On May 20, 1987, Eiseman: "Got $1 million authority" from National Union for the *Homestead* case." Centennial refused to contribute to the settlement because its primary policy did not cover the dates when the defamatory statements were made to the originators.

At the request of the PaineWebber attorneys, a meeting was set for June 12, 1987, with Beck and other Fireman's Fund executives. Keesal reiterated his appraisal of the case, stated that a settlement could be reached for $10 to $28 million and asked Fireman's Fund to contribute $3 or $5 million, depending on whether they waived certain subrogation rights. Keesal also announced that National Union was contributing $1 million, which was their policy limit, and that PaineWebber would contribute its own cash to a settlement. No one from Fireman's Fund asked significant questions or disagreed with Keesal's appraisal of the *Homestead*

case. The meeting ended with the Fireman's Fund representatives stating that they would discuss the matter and respond to Keesal.

On or about June 15, 1987, Schiff telephoned Keesal. Schiff stated that Fireman's Fund would not contribute, approve a settlement or be bound by a judgment of Judge Peckham. Fireman's Fund asserted clauses D and O and would "relitigate it in a subsequent action." Keesal proposed that Fireman's Fund participate in a settlement and reserve its right to litigate coverage. Schiff said "no."

Between June 15 and 18, 1987, Judge Peckham and the attorneys worked out a settlement in the *Homestead* case for $20,750,000. Judge Peckham declared that the settlement was fair. In a telephone call on June 18, Keesal informed Schiff of the settlement, mentioned that National Union was contributing $1 million and asked for a contribution of $5 million. Schiff replied that "he wasn't surprised" about the settlement. Schiff "thought the settlement was reasonable, that they were not going to participate." The only offer made by Schiff was that Fireman's Fund would buy back its policy for $500,000.

On June 20, 1987, Keesal sent a letter to Schiff by hand delivery which reiterated PaineWebber's position and restated their June 18 telephone conversation. Keesal also wrote that PaineWebber was contributing $18 million of its own money to the settlement and that Fireman's Fund appeared to be acting in bad faith.

On June 24, 1987, Schiff sent a letter to Keesal by hand delivery. The letter stated that National Union did not express its evaluation of the case to Fireman's Fund and "we do not rely on their decision." Further, Schiff claimed that Keesal had "repeatedly acknowledged" there was no evidence supporting a verdict for Homestead or any damages due to defamation. The sole basis urged by Keesal for settlement was that "Judge Peckham appeared to be 'senile,' and unable to follow [Keesal's] cross-examination and argument." Fireman's Fund again refused to provide any funds

because its observation of the trial indicated that the defamation damages fell below the policy limits.

On June 30, 1987, Keesal sent a letter to Schiff "vehemently" denying that Keesal ever conceded a lack of evidence of sufficient defamation damages and that the basis for a settlement was Judge Peckham's senility. The remainder of the letter set forth Keesal's consistently pessimistic evaluation of the case. Keesal testified that out of frustration with the way the *Homestead* case was proceeding, he might have used the word "senile" in conjunction with Judge Peckham at one of his meetings with insurance company representatives. However, "[i]t was not a major point." Boutin testified that Schiff mischaracterized the "senile" comment. In response to a request for admission, PaineWebber admitted that Judge Peckham was not senile. The phrase "barnyard equity" was used by Keesal in a deposition as a sort of glib shorthand phrase describing how he arrived at the figure of $3 million as the fair share to be paid by Fireman's Fund.

Also on June 30, 1987, PaineWebber executed a settlement agreement with *Homestead* for the sum of $20,750,000. The settlement was paid in full and covered all causes of action in the *Homestead* case.

A Fireman's Fund internal memorandum dated July 13, 1987, stated that the sender had "no record of having received a response from you to my April 2[] memorandum expressing our concerns over the handling of this high potential case." A July 16 letter from Woodard to the Keesal firm seems to indicate that Woodard was unaware of much of what had transpired since he transferred the case to the home office of Fireman's Fund. On July 31, 1987, Schiff wrote to Keesal stating that Homestead had a strong breach of contract claim, but a weak claim for defamation. Further, Homestead's "few" defamation witnesses did not establish damages above $1 million. Schiff again relied on policy conditions D and O to relieve Fireman's Fund of any liability for an unapproved settlement.

Attorney John Keker appeared as an expert witness for PaineWebber. After reading the reporter's transcript, briefs, depositions, pleadings and related items from the *Homestead* case, Keker reached the following opinions: (1) "the contract and tort legal theories apply basically to one set of facts giving rise to one set of damages []"; (2) "the defamation case was from [Homestead's] point of view off to a good start[]"; (3) the depositions indicated that PaineWebber's witnesses were not going to be able to "make much of a dent on this good slander case"; (4) Judge Peckham "didn't seem to be buying" PaineWebber's defenses; (5) there was "a real exposure to a defamation verdict against PaineWebber"; (6) based on the originator testimony, defamation damages would most likely be in the area of $30 million and no reasonable attorney could state that defamation damages could not exceed $1 million. Attorney Jerome Braun testified as an expert witness for Fireman's Fund and reached the opposite opinion from Keker based on the same documents.

Attorney and insurance industry consultant Stephen D. Prater also testified as an expert witness for PaineWebber. Based on reading the *Homestead* case documents, he reached the opinion that Fireman's Fund violated the implied covenant of good faith and fair dealing, along with Insurance Code section 790.03 which regulates unfair claims practices. Prater was especially critical of the failure of Beck to play a more active role in the investigation and evaluation of the insurance claim.

DISCUSSION

1. Standard of Review

An appellate court makes its own interpretation of the meaning of insurance policy provisions and is not bound by the interpretation of the trial court. (*Bank of the West* v. *Superior Court* (1992) 2 Cal.4th 1254, 1265) However, " '[w]hether the insurer has acted unreasonably, and hence in bad faith, in rejecting a settlement offer is a question of fact

to be determined by the jury.' [Citation.]" (*Walbrook Ins. Co.* v. *Liberty Mutual Ins. Co.* (1992) 5 Cal.App.4th 1445, 1454.)

Questions of fact are reviewed under the substantial evidence rule. "When a trial court's factual determination is attacked on the ground that there is no substantial evidence to sustain it, the power of an appellate court begins and ends with the determination as to whether, on the entire record, there is substantial evidence, contradicted or uncontradicted, which will support the determination, and when two or more inferences can reasonably be deduced from the facts, a reviewing court is without power to substitute its deductions for those of the trial court. If such substantial evidence be found, it is of no consequence that the trial court believing other evidence, or drawing other reasonable inferences, might have reached a contrary conclusion. [Citations.]" (*Bowers* v. *Bernards* (1984) 150 Cal.App.3d 870, 873-874, italics omitted.)

2. Substantial Evidence of $3 Million Covered Damages for Defamation

The jury reached special verdicts awarding PaineWebber $3,000,000 on "the issue of liability for the claim of [b]reach of the [d]uty of [g]ood [f]aith and [f]air [d]ealing ([b]reach of [c]ontract)." Total compensatory damages awarded to PaineWebber were $3,000,000. Fireman's Fund contends that the evidence in the *Homestead* case did not establish covered defamation damages of $3 million or of any sum over $1 million. This contention lacks merit.

Where an insurance carrier "fails to deal fairly and in good faith with its insured by refusing, without proper cause, to compensate its insured for *a loss covered by the policy,* such conduct may give rise to a cause of action in tort for breach of an implied covenant of good faith and fair dealing." (*Gruenberg* v. *Aetna Ins. Co.* (1973) 9 Cal.3d 566, 574, italics changed from original.) Failure to accept a reasonable settlement within policy limits can give rise to such cause of action. (*Id.* at p. 573.) It is undisputed that damages for

defamation are, and damages for breach of contract are not, covered by the Fireman's Fund excess policy in issue.

Civil Code section 46(3) provides: "Slander is a false and unprivileged publication, orally uttered, . . . which: Tends directly to injure [any person] in respect to his office, profession, trade or business, either by imputing to him general disqualification in those respects which the office or other occupation peculiarly requires, or by imputing something with reference to his office, profession, trade or business that has a natural tendency to lessen its profits." "A corporation can be libeled by statements which injure its business reputation. [Citations.]" (*Barnes-Hind, Inc.* v. *Superior Court* (1986) 181 Cal.App.3d 377, 381.)

Statements that a business "had moved its office and/or was closed, out of business, and unable to furnish goods and services" constituted slander per se, so that the business was not required to prove special damages in order to recover for damage to its reputation. (*Heritage Optical Center, Inc.* v. *Levine* (Mich. App. 1984) 359 N.W.2d 210, 211-213.) Likewise, damages to the reputation are presumed when the agent of a corporation falsely states that the corporation " 'was about to sell its entire business, was about to discontinue its business and was about to leave [its] field. . . .' " (*Edwards X-Ray Co.* v. *Ritter Dental Mfg. Co.* (1925) 210 N.Y.S. 299, 302.) Defamation per se was also established when the statements were that a food service business "was having financial problems" and "had almost been shut down by the health department." (*Mid-America Food Service* v. *ARA Services, Inc.* (8th Cir. 1978) 578 F.2d 691,698.)

"[C]overage under a liability insurance policy is equally available to an insured whenever an insured risk constitutes simply *a* concurrent proximate cause of the injuries. That multiple causes may have effectuated the loss does not negate any single cause; that multiple acts concurred in the infliction of injury does not nullify any single contributory act." (*State Farm Mut. Auto. Ins. Co.* v. *Partridge* (1973) 10 Cal.3d 94, 104-105, original italics, fn. omitted.) Where there are multiple causes for a loss, one of which is an included risk

and one which is an excluded risk, there is coverage if an independent concurrent proximate cause of the harm is an included risk under the terms of the policy. (*Gurrola* v. *Great Southwest Ins. Co.* (1993) 17 Cal.App.4th 65, 68.) (The decisions in *State Farm Mut. Auto. Ins. Co.* v. *Partridge* was limited to cases involving liability insurance in *Garvey* v. *State Farm Fire & Casualty Co.* (1989) 48 Cal.3d 395, 398-399, 411-412, fn. 10. See *Mission National Ins. Co.* v. *Coachella Valley Water Dist.* (1989) 210 Cal.App.3d 484, 491.) Thus, an act of defamation, which also breaches a contract, is covered if defamation otherwise gives rise to liability under the provisions of an insurance policy. (*Boston Symphony* v. *Commercial Union Ins.* (Mass. 1989) 545 N.E.2d 1156, 1159.)

When an insurance carrier wrongly denies coverage, the amount of a reasonable settlement of the claim may be used as presumptive evidence of the damages owed by the carrier. (*Isaacson* v. *California Ins. Guarantee Assn.* (1988) 44 Cal.3d 775, 791.)

The statements made by PaineWebber representatives about Homestead, as described by the originators, are almost identical to the statements characterized as defamation per se in the above cases. Further, the actual and proposed originator testimony established that Homestead ceased to obtain any more government loan business under its contract with PaineWebber after April 12, 1985, because of the statements by PaineWebber. Thus, the false statements that Homestead was out of the loan business were acts of defamation which also breached the contract between the two businesses. Damage experts testified that the business profits lost by Homestead from the failure to obtain government loans through PaineWebber totaled between $85 and $158 million. Liability for defamation was admittedly a risk covered by the policy. Under the doctrine of concurrent causation these damages, which flowed directly from the statements, were covered risks. The $3 million compensatory damages awarded by the jury is supported by evidence that

Fireman's Fund unreasonably refused to contribute such sum to the settlement on the ground that its policy did not cover any liability arising from the Homestead case.

3. Policy Conditions D and O

Conditions D and O of the Fireman's Fund excess policy stated that the company shall only be liable for payment after a judgment, or settlement agreement entered into with its written consent. Fireman's Fund contends it "was entitled to rely on the express terms of the Fireman's Fund policy and require an adjudication of the claimed covered damages prior to any contribution to an unauthorized settlement." This contention lacks merit.

In 1963, *Kelley* v. *British Com. Ins. Co.* (1963) 221 Cal.App.2d 554, 563 rejected an argument similar to Fireman's Fund's by holding that an excess carrier "was obviously under a duty to exercise good faith towards its insured in considering any offer of compromise within the limits of its policy."

In 1979, *Transit Casualty Co.* v. *Spink Corp.* 1979) 94 Cal.App.3d 124, 136, which involved an excess insurer, held: "There is however a public interest in extrajudicial settlement of lawsuits. [Citations.] The settlement clause tends to defeat that interest and therefore will be narrowly construed so as not to defeat the covenant of good faith and fair dealing which is an implied reciprocal term of the policy. That covenant contemplates that neither party will injure unreasonably, and certainly not arbitrarily, the right of the other to receive the benefit of the agreement or to minimize a loss thereunder. [Citation.] [¶] Thus the settlement clause does not permit unreasonable rejection of settlement by the insured." This portion of *Transit Casualty* was affirmed by the Supreme Court in *Commercial Union Assurance Companies* v. *Safeway Stores, Inc.* (1980) 26 Cal.3d 912, 921, and *Signal Companies, Inc.* v. *Harbor Insurance Co.* (1980) 27 Cal.3d 359, 365. Other portions were disapproved.

In *Diamond Heights Homeowner's Assn.* v. *National American Ins. Co.* (1991) 227 Cal.App.3d 563 (*Diamond*

Heights Homeowner's Assn.), this court, per Strankman, J., Merrill, Acting P.J. and Chin, J., applied the rule of the above cases to a situation remarkably similar to the facts herein. Primary carriers paid the costs of defense and contributed to the settlement of a third party plaintiff's action against the insured. An excess carrier refused to contribute to or approve of the settlement. In a subsequent action by the insured against the excess carrier, the latter defended in part on the ground that a settlement without its consent violated a condition of the policy. The policy also gave the excess carrier the right to participate in the defense. (*Id.* at pp. 570, 573, 575.)

This court rejected the excess carrier's defense as follows: "Any insurer, whether excess or primary, in conducting settlement negotiations, is subject to an implied duty of good faith and fair dealing which requires it to consider the interests of the insured equally with its own and evaluate settlement proposals as though it alone carried the entire risk of loss. [Citations.]" (*Diamond Heights Homeowner's Assn., supra,* at p. 578) The insured is not required to demand that the excess carrier undertake the defense of the action prior to entering into the settlement. (*Id.* at p. 579.) An excess carrier "may waive its rights under [the consent to settlement] clause if it rejects a reasonable settlement and at the same time fails to offer to undertake the defense." (*Id.* at p. 581, original italics.) Even if the maximum potential liability of the insured does not exceed the limits of the excess policy, the excess carrier does not have an absolute right to object to the settlement. (*Id.* at pp. 581-582.) These holdings of *Diamond Heights Homeowners Assn.* were approved in subsequent Court of Appeal cases which disagreed with other aspects of the opinion not involved in the instant case. (See *Pruyn* v. *Agricultural Ins. Co.* (1995) 36 Cal.App.4th 500, 524-525, 531 and our opinion per Chin, P.J., Merrill, J. and Corrigan, J. in *Hartford Accident & Indemnity Co.* v. *Superior Court* (1995) 37 Cal.App.4th 1174, 1180-1184.)

We reaffirm the relevant holdings in *Diamond Heights Homeowners Assn.*, which follow a 33-year line of Supreme

Court and Court of Appeal cases. Accordingly, Fireman's Fund did not escape liability merely by refusing to consent to the settlement in the *Homestead* case. Additionally, we agree with Judge Peckham and Fireman's Fund attorney Schiff that the settlement was fair and reasonable. Moreover, as more fully discussed in section 2 of this discussion, the settlement covered liability for defamation and breach of contract. Thus, Fireman's Fund could not properly withhold its consent.

Fireman's Fund also relies on *Finkelstein* v. *20th Century Ins. Co.* (1992) 11 Cal.App.4th 926, 929, which held: "[A]n insurance company is liable to an insured when the insurer unreasonably refuses to settle the case within the insured's policy limits *and* a 'judgment' in excess of those limits is ultimately rendered against the insured." [Citation.]" (Original italics.) The principal case cited by Finkelstein in support of its conclusion is *Comunale* v. *Traders & General Ins. Co.* (1958) 50 Cal.2d 654, 661 (*Comunale*); however, no analysis of *Comunale* was conducted.

Camelot By The Bay Condominium Owners' Assn. v. *Scottsdale Ins. Co.* (1994) 27 Cal.App.4th 33, 46-49, carefully analyzed the *Comunale* line of cases and concluded that the requirements for insurer liability for breach of the covenant of good faith and fair dealing for failure to settle are as follows: "(1) [U]ltimately, coverage must be found to exist [citation]; (2) [t]he most reasonable method of resolving a claim is evaluated in light of the probability or risk at settlement time of an excess judgment against the insured [citation.]; (3) an unavoidable additional factor in the insurer's 'reasonableness analysis' of the settlement decision is whether it may potentially be exposed to additional damages to its insured for any failure to settle [citation]; and (4) when the settlement decision must be made, the insurer may not allow coverage beliefs or policy limits to control the settlement decision [citation]. . . . Finally there is no explicit requirement for bad faith liability that an excess judgment is actually suffered by the insured, since the reasonableness analysis of settlement decisions is performed in terms of the

probability or risk that such a judgment may be forthcoming in the future. . . ." We are persuaded by the reasoning and conclusions of *Camelot By The Bay.*

4. Substantial Evidence of Bad Faith

The jury reached special verdicts awarding PaineWebber $3,000,000 on "the issue of liability for the claim of [b]reach of the [d]uty of [g]ood [f]aith and [f]air [d]ealing ([t]ort), . . ." It also found in favor of PaineWebber on the issue of PaineWebber's "Comparative Bad Faith." Total compensatory damages awarded to PaineWebber were $3,000,000. Fireman's Fund contends the evidence establishes that (even) if it was wrong about coverage it did not act in bad faith. This contention lacks merit.

"It is now clear under California law that an insurer's erroneous failure to pay benefits under a policy does not necessarily constitute bad faith entitling the insured to recover tort damages." The refusal to pay must be "unreasonable" and "without proper cause." (*Opsal* v. *United Services Auto. Assn.* (1991) 2 Cal.App.4th 1197, 1205.) "[B]ad faith liability cannot be imposed where there exist[s] a genuine issue as to [the insurer's] liability under California law.' [Citation.]" (*Id.* at pp. 1205-1206.)

"[T]he litmus of good faith/bad faith is to be tested against the background of the totality of the circumstances in which the insurer's actions occurred. [Citations.]" (*Walbrook Ins. Co.* v. *Liberty Mutual Ins. Co., supra,* 5 Cal.App.4th at pp. 1455-1456.) "[M]otive, intent and state of mind" are the key factors. Bad faith is indicated when an insurance carrier refuses to settle within policy limits and "there is a substantial likelihood of a recovery in excess of those limits," or where the third-party plaintiff's case is comparatively strong and insured's defense has a weak potential. The carrier must conduct a reasonable investigation. Its own personnel must carefully weigh settlement offers and not reach a decision based on "close-fisted intractability." (*Id.* at pp. 1454, 1456-1458, citations and internal quotation marks omitted.) An insurance carrier's "figurative hiding its head in the sand (or

hiding adverse reports) is not a law-sanctioned approach to reasonable investigation and performance of its duty." (*Betts* v. *Allstate Ins. Co.* (1984) 154 Cal.App.3d 688, 707.)

Each of the above-listed bad faith factors is present herein. Unlike representatives of the primary carriers, Beck, the "point person" for Fireman's Fund, intentionally abdicated responsibility for the *Homestead* case. Additionally, Fireman's Fund internal memoranda disclose that the state of mind of its executives was confusion over what was happening with a multi-million dollar case against its insured.

PaineWebber's attorneys provided Fireman's Fund with the multifarious documents generated in the trial and explained to them why there was a substantial likelihood Homestead would prevail. These documents, especially the transcript of the originator testimony, fully supported the reports from PaineWebber's attorneys that a settlement was appropriate because Homestead's case was comparatively strong and PaineWebber's defense had weak potential. Solid evidence also supported damages well in excess of Fireman's Fund's policy limits of $25 million.

At no time did the attorneys for Fireman's Fund challenge PaineWebber's pessimistic assessment of the case. Fireman's Fund's attorneys even agreed that the settlement for $20,750,000 was fair. The only objection raised by Fireman's Fund was that Homestead had only established a breach of contract case. However, no genuine issue of liability was raised because long-standing legal authorities, which are virtually unchallenged, established without question that in the *Homestead* case the breach of contract and defamation claims, as well as the defenses thereto, were identical since the contract was breached by the defamatory statements. Damages for both claims were also identical under the law.

Thus, the totality of Fireman's Fund's conduct exhibited a blatant disregard for its insured, PaineWebber, and for the seriousness of Homestead's case. Fireman's Fund acted unreasonably. The only explanation for its conduct was that it

hid its head in the sand or was solely motivated by close-fisted intractability. For all these reasons the evidence supports the jury's verdict in favor of bad faith tort damages.

5. Expert Witnesses

Fireman's Fund contends expert testimony was improperly admitted in the instant case and that "PaineWebber should have been required to try the *Homestead* case within this case, . . ." This contention lacks merit.

Fireman's Fund exclusively relies on *Travelers Ins. Co.* v. *Lesher* (1986) 187 Cal.App.3d 169 (*Travelers*). Throughout the opinion, the *Travelers* court recognized the unique nature of the case: "Lesher's theory of liability at trial was not dependent on a determination that Travelers had a duty to defend or indemnify under the terms of the policy. Instead Lesher's theory was as follows. Despite the coverage dispute, once Travelers undertook Lesher's defense, it was obligated to conduct that defense with the same duty of care as if there were no coverage dispute. . . . Neither party has cited any case in which liability has been imposed on an insurer under similar facts." (*Id.* at p. 187.)

The principal language relied on by Fireman's Fund holds: "We are aware of no California cases which hold that in an attorney malpractice action, expert testimony alone would suffice to prove the outcome of the underlying case. Given the similarity between attorney malpractice cases and Lesher's unique theory of damages in this case, we conclude that he should have been required to try the underlying Worrell antitrust action within this bad faith action to sustain his claim that he would have successfully defended the Worrell action but for Travelers' acts and omissions." (*Id.* at p. 197.)

The instant case does not arise from a unique theory. It is a traditional bad faith/duty to indemnify case. Expert evidence is admissible in this type of case (*Neal* v. *Farmers Ins. Exchange* (1978) 21 Cal.3d 910, 924 (*Neal.*) Also, none of the many bad faith refusal to settle cases that we have reviewed

require a trial of the underlying case. Thus, *Travelers Insurance* does not govern the instant case. Moreover, the jury did not decide on the basis of "expert evidence alone." The entire reporter's transcript of the *Homestead* case was introduced into evidence and Boutin testified extensively about the *Homestead* case.

6. Basis For Punitive Damages

Regarding punitive damages liability, the jury found "by clear and convincing evidence" that Fireman's Fund acted with malice, but not oppression or fraud. Appellant contends that "Fireman's Fund's claim handling, and particularly its decision not to accede to a $3,000,000 demand based on 'barnyard equity', was neither malicious nor reprehensible. . . ." This contention lacks merit.

A determination that the defendant carrier acted with bad faith "does not in itself establish that defendant acted with the quality of intent that is requisite to an award of punitive damages. For this we must look further—beyond the matter of reasonable response to that of motive and intent." A jury can find the requisite malice from especially grievous acts of bad faith. (*Neal, supra,* 21 Cal.3d 910 at pp. 922-923.

Examples of specific conduct which tends to establish malice are as follows: taking advantage of the exigent financial situation of an insured (*Neal, supra,* 21 Cal.3d at pp. 922-923); "the insurer wil[l]fully and deliberately failed to take the steps necessary to avoid the adverse consequences that the unwarranted denial of its claim would have." (*Delgado* v. *Heritage Life Ins. Co.* (1984) 157 Cal.App.3d 262, 277); interpreting a policy in a "restrictive manner" and failing to conduct an investigation (*id.* at p. 278). Further, an insurance company commits "tortious misconduct" by placing conditions on its payment of policy proceeds. (*Mock* v. *Michigan Millers Mutual Ins. Co.* (1992) 4 Cal.App.4th 306, 325.) When a judgment in excess of policy limits is likely, the prudent course of action is for the insurer to accept a proffered settlement within policy limits and litigate the issue of

coverage with its insured later. (*Johansen* v. *California State Auto Assn. Inter-Ins. Bureau* (1975) 15 Cal.3d 9, 12, 19.)

In the instant case, the conduct of Fireman's Fund was especially egregious because substantial evidence discloses that it completely disregarded the long-established law, testimony in the *Homestead* case, evaluation of the attorneys who were present at the trial, evaluation of the primary carrier and its own internal guidelines as to how to conduct an investigation. Further, we observe that PaineWebber did not demand that Fireman's Fund contribute to the settlement on the basis of "barnyard equity." The tendency of Fireman's Fund to seize upon passing phrases by the Keesal firm, such as "barnyard equity" or "senility" as the basis for their refusal to contribute, while at the same time ignoring persuasive, valid arguments, is itself a basis for the verdict of malice. Fireman's Fund also seriously mischaracterized the position of the attorneys for PaineWebber.

Further, the malicious intent and motive of Fireman's Fund is highlighted by its restrictive interpretation of Conditions D and O. It wrongly insisted that it could unreasonably refuse to approve of any settlement and need not pay until a judgment issued in favor of Homestead. At the same time it refused to be bound by a judgment that found defamation damages covered by the excess policy. Fireman's Fund refused to contribute to the settlement and reserve the coverage dispute for future litigation. Its only response was to take advantages of PaineWebber's adverse position and offer a sum below the policy minimum as complete satisfaction of its obligation. Accordingly malice was established and punitive damages were appropriate.

7. Amount of Punitive Damages

In the second part of a three-stage trial the jury awarded PaineWebber punitive damages in the amount of $21,000,000. The jury based its verdict on the evidence of Fireman's Fund's conduct described above and additional evidence that the actual net worth of Fireman's Fund was $2,690,000,000. Fireman's Fund filed motions for a judgment

notwithstanding the verdict or for a new trial. Memoranda in support of each motion argued that the punitive damages were excessive. At the hearing on the motions, Fireman's Fund argued that the damages were excessive, while PaineWebber argued to the contrary. The trial court denied both motions without comment.

Fireman's Fund contends: "Punitive damages four times as large as the largest award affirmed in a reported California opinion are grossly excessive as a matter of law." "In determining whether an award of punitive damages is excessive, comparison of the amount awarded with other awards in other cases is not a valid consideration. [Citations.] Nor does '[t]he fact that an award may set a precedent by its size' in and of itself render it suspect; whether the award was excessive must be assessed by examining the circumstances of the particular case. [Citations.]" (*Grimshaw* v. *Ford Motor Co.* (1981) 119 Cal.App.3d 757, 819.) In *West American Insurance Co.* v. *Freeman* (1995) 46 Cal.App.4th 1476, review granted and subsequently dismissed as "improvidently granted," Division Four of this district held that an award of punitive damages in the amount of $12 million was not excessive. Accordingly, we reject the argument of Fireman's Fund.

The decision of a trial court and jury on punitive damages is "accorded great weight" and will be reversed as excessive " 'only when the entire record viewed most favorably to the judgment indicates the award was rendered as the result of passion and prejudice. [Citation.]' [Citations.]" No single formula exists for calculating punitive damages. (*Devlin* v. *Kearny Mesa AMC/Jeep/Renault, Inc.* (1984) 155 Cal.App.3d 381, 388 *(Devlin)*. "The factors to be considered in assessing a punitive damages award are the nature of the defendant's acts, the amount of compensatory damages awarded and the wealth of the defendant. [Citation.]" (*Id.* at p. 389.)

Because the purposes of punitive damages are to punish the wrongdoer and to make an example of him, the wealthier the wrongdoer, the larger the award of punitive damages. (*Bertero* v. *National General Corp.* (1974) 13 Cal.3d 43, 65.)

"Net worth generally is considered the best measure of a defendant's 'wealth' for purposes of assessing punitive damages. [Citation.]" (*Devlin, supra,* 155 Cal.App.3d at p. 391.) There is no fixed ratio to determine the proper proportion between punitive and compensatory damages. [Citations.]" Ratios of 2,000:1, 74:1, 25.6:1 and 17.1:1 have been upheld. (*Id.* at pp. 393-396.)

All of the above factors support the award in the present case. The cavalier manner in which Fireman's Fund treated its insured regarding the "high potential" *Homestead* case was reprehensible. Large corporations such as PaineWebber have the same right to be treated fairly as do insureds of less means. A ratio of 7:1 between compensatory and punitive damages is well within the acceptable limits. Damages of $21 million are adequate, but not excessive, to punish a company as wealthy as Fireman's Fund. (See *Downey Savings & Loan Assn.* v. *Ohio Casualty Ins. Co.* (1987) 189 Cal.App.3d 1072, 1099-1100 [affirming punitive damages award of 1.9 percent of the defendant's net worth].) In an inflationary economy, such as ours has been since the end of World War II, punitive damages may continue to grow as defendants' net worth grows larger, at least on paper. Without going into complicated mathematical/economic formulas, we suspect that in real economic terms the damages herein might well be of the same magnitude as those in earlier cases.

8. Instructions

Fireman's Fund contends that several jury instructions were erroneous. None of the challenges have merit.

Contrary to the argument of Fireman's Fund, the instruction that Fireman's Fund cannot reject a "reasonable settlement" is a correct statement of law for the reasons stated under section 3 of this discussion. For the same reasons, instruction number 108 proposed by Fireman's Fund was improper. The instruction forbidding the parties from calling witnesses from the *Homestead* case to testify about the facts of that case was proper for the reasons stated under section 5 of this discussion. For the reasons stated under section 2

above, the instructions regarding the covenant of good faith and fair dealing properly implied that Homestead's claims against PaineWebber were fully covered and would have resulted in an excess judgment.

Fireman's Fund contends that the trial court failed to adequately instruct the jury regarding the high level of proof required to meet the "clear and convincing" standard for punitive damages.

BAJI No. 2.62 (8th ed. 1994 bound vol.) defines "clear and convincing" as follows: " 'Clear and convincing' evidence means evidence of such convincing force that it demonstrates, in contrast to the opposing evidence, a high probability of the truth of the fact[s] for which it is offered as proof. Such evidence requires a higher standard of proof than proof by a preponderance of the evidence. [¶] You should consider all of the evidence bearing upon every issue regardless of who produced it."

Fireman's Fund proposed that the trial court give a different definition: " 'Clear and convincing' evidence requires a finding of high probability. The evidence must be so clear as to leave no substantial doubt and must be sufficiently strong to command the unhesitating assent of every reasonable mind."

Instead, the trial court instructed as follows: " 'Clear and convincing' evidence means evidence which can be direct or circumstantial, of such convincing force that it demonstrates, in contrast to the opposing evidence, a high probability of the truth of the facts for which it is offered as proof. Such evidence requires a higher standard of proof than proof by a preponderance of the evidence. It is evidence that is clear, explicit, and unequivocal."

In re Marriage of Weaver (1990) 224 Cal.App.3d 478, 487, footnote 8 criticized BAJI No. 2.62 as "misleading and unnecessarily limited" and opined that "it seems to suggest an evidentiary test which is significantly less rigorous than the one which the Supreme Court has repeatedly characterized

as requiring evidence which is 'clear, explicit, and unequivocal,' 'so clear as to leave no substantial doubt' and sufficiently strong to command the unhesitating assent of every reasonable mind." (Some internal quotation marks omitted.) In *Weaver,* the court's comments on BAJI No. 2.62 were dicta because the court was simply providing guidance to the trial court on retrial as to the proper standard of proof. (See also *Mock* v. *Michigan Millers Mutual Ins. Co.* (1992) 4 Cal.App.4th 306, 332-333 and *Dubarry Internat., Inc.* v. *Southwest Forest Industries, Inc.* (1991) 231 Cal.App.3d 552, 566, fn. 19 [in dicta, the Second District, in opinions authored by Justice Croskey, similarly criticizes BAJI No. 2.62].) We conclude that the modifications made by the trial court satisfy the criticisms of *Weaver* and the other cases.

Fireman's Fund contends that the "instructions regarding one of the causes of action—breach of statutory duties [Insurance Code section 790.03 et seq.]—was completely erroneous, since the Supreme Court has ruled that no such cause of action can be maintained against an insurer for failing to settle a claim against its insured unless that claim proceeded to final judgment." The case cited is *Moradi-Shalal.* v. *Fireman's Fund Ins. Companies* (1988) 46 Cal.3d 287. In *Moradi-Shalal* the Supreme Court overruled its previous case of *Royal Globe Ins. Co.* v. *Superior Court* (1979) 23 Cal.3d 880, which allowed statutory actions, and held, at page 313, that "as to cases filed prior to finality of our opinion herein, . . . the insured's liability must be judicially determined before a [statutory] action can be brought."

Moradi-Shalal was decided in August 1988 and only prohibits "third party" actions filed after that date. It does not prohibit "first party" statutory actions filed at any time. (*Xebec Development Partners, Ltd.* v. *National Union Fire Ins. Co.* (1993) 12 Cal.App.4th 501, 573-574.) Herein, the complaint was filed by an insured against its carrier on February 23, 1988. Accordingly the statutory causes of action were preserved.

9. Attorney Fees

After a court trial, the trial court issued a detailed statement of decision which awarded PaineWebber attorney fees of $1,511,444.46 and costs of $307,675.47, for a total of $1,819,119.93. Prejudgment interest of $2,840,393.32 was also awarded. Fireman's Fund contends that no fees, costs, or interest should have been awarded and that the amounts are excessive. These contentions lack merit.

Brandt v. *Superior Court* (1985) 37 Cal.3d 813, holds: "When an insurer's tortious conduct reasonably compels the insured to retain an attorney to obtain the benefits due under a policy, it follows that the insurer should be liable in a tort action for that expense. The attorney[] fees are an economic loss—damages—proximately caused by the tort. [Citation.] These fees must be distinguished from recovery of attorney[] fees *qua* attorney[] fees, such as those attributable to the bringing of the bad faith action itself." (*Id.* at p. 817.) "The fees recoverable, however, may not exceed the amount attributable to the attorney's efforts to obtain the rejected payment due on the insurance contract. Fees attributable to obtaining any portion of the plaintiff's award which exceeds the amount due under the policy are not recoverable." (*Id.* at p. 819)

As we have specified in detail above, the tortious conduct of Fireman's Fund compelled PaineWebber to retain attorneys to obtain the benefits due under the policy.

The trial court's statement of decision relates that PaineWebber "rendered monthly bills for legal fees and costs" in the amount of $1,758,857.25. Various sums were deducted from that amount. Regarding deductions of fees incurred exclusively for punitive damages or other theories not directly related to obtaining policy benefits, the statement of decision declares: "All of the claims in this case irrespective of their legal [labeling], involved a common core of operative facts. Moreover, virtually all of the legal fees and costs claimed were necessarily incurred to recover policy benefits. Under these circumstances, all of the fees in this case arguably are recoverable under *[Brandt]*. Nonetheless,

the [c]ourt, to be conservative, has made an allocation of fees in recognition of the fact that PaineWebber pursued several purely tort theories of recovery (i.e., fraud and breach of fiduciary duty). The [c]ourt has therefore made any deductions necessary under *[Brandt]* from a review of the evidence presented during the attorney[] fees portion of the trial in the form of testimony and exhibits entered into evidence, from the [c]ourt's observations of the actual trial, and from a review of the official [c]ourt docket in this matter. Based upon all of the above, the [c]ourt finds that the amount of $78,611.00 should be deducted from the total attorney[] fees recoverable."

" 'The "experienced trial judge is the best judge of the value of professional services rendered in [her] court, and while [her] judgment is of course subject to review, it will not be disturbed unless the appellate court is convinced that it is clearly wrong." [Citations.]' [Citation.]" (*Margolin* v. *Regional Planning Com.* (1982) 134 Cal.App.3d 999, 1007 (*Margolin*).) We agree with the statement of decision that all claims made by PaineWebber were closely interrelated and based on "a common core of operative facts." Accordingly, nothing in the record indicates that the trial judge, who presided over the entire case, abused her discretion in calculating the award of attorney fees.

Finally, Fireman's Fund contends that under *Xebec Development Partners, Ltd.* v. *National Union Fire Ins. Co., supra,* 12 Cal.App.4th 501, PaineWebber should be denied attorney fees and costs which were based on bills that had been "redacted" to preserve the attorney-client privilege. *Xebec* involves a trial court's award of attorney's fees based on bills subject to a privilege. At page 569 it held that the appellate court "cannot quibble with the disposition the trial court reached" because the trial court has "broad inherent powers to control" the use of privileged materials in presenting evidence of attorney fees. Moreover, on a similar contention the court in *Margolin, supra,* 134 Cal.App.3d at page 1006: "Appellants' contention is really one of insufficient evidence to support the court's judgment. As such, it fails since all hours

allegedly worked by counsel for which no time records were available were attested to by the attorneys under oath."

Herein the contention also fails, because all the hours in question were attested to by bills which gave some indication of the purpose of the services and testimony under oath.

DISPOSITION

The judgment is affirmed. Costs are awarded to PaineWebber.

Patsey, J.*

We concur:

Parrilli, Acting P.J.

Walker, J.

* Judge of the Contra Costa County Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

NOT TO BE PUBLISHED IN OFFICIAL REPORTS

In The Court Of Appeal

OF THE

State Of California

FIRST APPELLATE DISTRICT
DIVISION THREE

PAINEWEBBER REAL ESTATE SECURITIES, INC., et al.,
Plaintiffs and Respondents,

v.

FIREMAN'S FUND INSURANCE COMPANY, INC.,
Defendant and Appellant.

A063060

(City and County of San Francisco Super. Ct. No. 888592)

ORDER DENYING REHEARING AND CERTIFICATION FOR PUBLICATION

FILED
Court of Appeal-First App. Dist.
FEB - 3 1997
RON D. BARROW, CLERK
By_____
DEPUTY

BY THE COURT:

The requests for publication and the petition for rehearing are denied.

Dated: FEB 03 1997

PHELAN, J. P.J.

APPENDIX B

First Appellate District, Division Three, No. A063060
S059054

In The Supreme Court Of California

PAINE WEBBER REAL ESTATE SECURITIES INCORPORATED Et Al.,
Respondents

v.

FIREMAN'S FUND INSURANCE COMPANY,
Appellant

SUPREME COURT
FILED
MAR 26 1997
Robert Wandruff Clerk
DEPUTY

Appellant's petition for review DENIED.
The requests for an order directing publication of the opinion are denied.

GEORGE
Chief Justice

APPENDIX C

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Attorneys for Defendant
FIREMAN'S FUND INSURANCE COMPANY

Superior Court Of California

FOR THE

City And County Of San Francisco

PAINEWEBBER REAL ESTATE SECURITIES, INC., PAINEBEBBER INC. AND PAINEWEBBER MORTGAGE FINANCE
Plaintiffs,

vs.

FIREMAN'S FUND INSURANCE COMPANY, INC., a California corporation,
Defendant.

Case No. 888592

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT FIREMAN'S FUND INSURANCE COMPANY'S MOTION FOR NEW TRIAL

Date: To be Determined
Time: 8:00 a.m.
Dept: The Honorable Anne Bouliane, Dept. 30
[Sitting as Dept. 7]

APPENDIX D

unjustified punitive damage award, FIREMAN'S FUND has been subjected to punishment over and above any possible compensatory obligation, and PAINEWEBBER has been richly rewarded for defaming and breaching its contract with Homestead. FIREMAN'S FUND submits that the excessive and unjustified punitive damage award in this action merits a new trial so that FIREMAN'S FUND's conduct, and not its financial condition, can be appropriately evaluated.

B. Notwithstanding The Absence Of Any Legal Or Factual Basis For The Punitive Damage Award, The California Standard Of Review For Punitive Damages Is Unconstitutional Under The United States And California Constitutions.

Recently, the United States Supreme Court addressed the constitutionality of a punitive damage award in *Pacific Mutual Ins. Co. v. Haslip* (1991) 499 U.S. 1, 111 S. Ct. 1032, 113 L. Ed. 2d 1. In *Haslip,* the United States Supreme Court upheld a punitive damage award by an Alabama jury because the Alabama Supreme Court's substantive standards for review of such awards "impose a sufficiently definite and meaningful constraint on the discretion of Alabama fact finders in awarding punitive damages". *Haslip,* 499 U.S. at , 111 S. Ct. at 1045, 113 L. Ed. 2d at 22. In Alabama, a punitive damage award is subject to a review of seven specific objective factors, "to ensure that the award does not exceed an amount that will accomplish society's goals of punishment and deterrence". *Id.*

Unlike Alabama, California has no system of independent review of punitive damage awards, which is crucial to affording due process. The California standard is applied by the courts only to determine whether the jury acted out of "passion or prejudice" in making a punitive damage award. Unlike the Alabama standard of review, the California standard does not employ objective factors, and does not provide adequate and specific protection against an excessive award. Nor does it examine whether a particular award is tailored to accomplish society's goals of punishment and deterrence. Id.

Indeed, California deliberately has vague standards to encourage subjective results. *Devlin* v. *Kearney Mesa AMC/Jeep/Renault* (1984) 155 Cal.App.3d 381, 388, 202 Cal.Rptr. 204, 209.

In light of *Haslip,* the California standard of review, which accords undue deference to the jury's discretion, is no longer adequate to satisfy federal or state constitutional due process. Interestingly enough, shortly after its decision in *Haslip,* the United States Supreme Court remanded seven cases, including three from California,[14] for further proceedings to determine whether the punitive damages awarded in those cases met the constitutional standards delineated in *Haslip.* Based on a standard of review in California which is unconstitutional after *Haslip,* FIREMAN'S FUND contends that the punitive damage award must not be allowed to stand without benefit of a new trial.

In *Haslip,* the United States Supreme Court observed, consistent with the California Supreme Court, that punitive damage awards should bear a reasonable relation, and not a disproportionate ratio, to compensatory damages as discussed by FIREMAN'S FUND in Section A above. The jury award against FIREMAN'S FUND far exceeds even the 4 to 1 ratio which the United States Supreme Court stated was "close to the line" and allows PAINEWEBBER to reap the windfall which *Haslip* and the above-referenced California decisions specifically prohibit. The excessiveness of the punitive damage award, along with PAINEWEBBER's attempts to single out an insurer such as FIREMAN'S FUND to shoulder its financial burdens[15], effectively deny FIREMAN'S FUND its right to due process under the Fourteenth

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[14] *International Society for Krishna Consciousness* v. *George,* 499 U.S. _____, 111 S. Ct. 1299, 113 L. Ed. 2d 234 (1991); *Church of Scientology* v. *Wollersheim,* 499 U.S. _____, 111 S. Ct. 1298, 113 L. Ed. 2d 234 (1991); *Pacific Lighting Corp.* v. *MGW, Inc.,* 499 U.S. _____, 111 S. Ct. 1299, 113 L. Ed. 2d 235 (1991).

[15] *See, California Physicians' Service* v. *Superior Court* (1992) 9 Cal.App.4th 1321, 12 Cal.Rptr.2d 95 [rejecting argument that "insurance

Amendment of the United States Constitution and Article I, 7(a) of the California Constitution.

VI. THE AWARD OF ATTORNEYS' FEES ALSO IS EXCESSIVE BECAUSE, AS RECENT APPELLATE AUTHORITY CONFIRMS, PAINEWEBBER CANNOT RECOVER ATTORNEYS' FEES WHERE THE PRIVILEGE HAS BEEN ASSERTED TO PREVENT DISCLOSURE OF THE WORK WHICH HAS BEEN PERFORMED.

As the Court will recall, FIREMAN'S FUND repeatedly has urged that PAINEWEBBER could not refuse to disclose (on the basis of privilege) the work its lawyers performed and still prove those fees were recoverable under *Brandt v. Superior Court* (1985) 37 Cal.3d 813, issue a written decision articulating the Court's reasons for upholding, modifying or reversing the punitive damage award.

DATED: July 12, 1993

Respectfully submitted,

HAIGHT, BROWN & BONESTEEL

FISHER & HURST

By: /S/

LORI A. SEBRANSKY
Attorneys for Defendant
FIREMAN'S FUND
INSURANCE COMPANY

---

company defendants who have engaged in bad faith denial of claims do not have the same privileges in terms of fensive pleadings as do other defendants"].

PROOF OF SERVICE

I declare that:

I am employed in the County of San Francisco, California. I am over the age of eighteen years and not a party to the within cause. On July 12, 1993 I served the within DEFENDANT FIREMAN'S FUND INSURANCE COMPANY'S MOTION FOR NEW TRIAL AND MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF THEREOF on the parties in said cause by hand delivering a true and correct copy thereof to:

James Bennett, Esq.
MORRISON & FOERSTER
345 California Street
San Francisco, Ca 94104

Honorable Anne Bouliane [Courtesy Copy]
Superior Court Judge
San Francisco Superior Court
375 Woodside Road
Department 30
San Francisco, California

I declare under penalty of perjury that the foregoing is true and correct, and that this declaration was executed on July 12, 1993 at San Francisco, California.

1ST CIVIL NO.

A06306

In The Court Of Appeal

OF THE

State Of California

FIRST APPELLATE DISTRICT
DIVISION THREE

PAINEWEBBER REAL ESTATE SECURITIES, INC.,
PAINEWEBBER GROUP, INC.,
PAINEWEBBER GROUP, INCORPORATED, and
PAINEWEBBER MORTGAGE FINANCE, INC.,
Plaintiffs and Respondents,

v.

FIREMAN'S FUND INSURANCE COMPANY, INC.,
Defendant and Appellant.

Superior Court of California, County of San Francisco
Case Number 888592
Honorable Anne Bouliane, Judge

APPELLANT'S PETITION FOR REHEARING

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APPENDIX E

III. THE INSUFFICIENCY OF THE PUNITIVE DAMAGES REVIEW

Nationwide, cases applying the eight-month old *BMW* decision show that other courts understand that the *BMW* case created a standard against which to judge the reprehensibility of a defendant's conduct for punitive damages purposes. However, none of these factors were considered by the Court here. This is especially ironic since these factors are essentially identical to the objective factors utilized by California courts to evaluate the excessiveness of punitive damages.

Firemans Fund alleged misconduct was never subjected to any "meaningful judicial scrutiny" that applied these objective criteria. *Adams,* 54 Cal. 3d at 118. Such scrutiny would have shown a *single* "wrongful" incident rather than repeated misconduct or a wrongful corporate policy. Such scrutiny would have shown that PaineWebber was a wealthy and sophisticated plaintiff rather than a vulnerable consumer insured. Finally, such scrutiny would have shown, at most, economic harm, rather than harm to the health or safety of individuals. In short, such scrutiny would have demonstrated that the degree of reprehensibility here fails to justify the size of the punitive damages award.

A. The BMW Case Has Been Followed Nationwide.

Courts nationwide have followed the factors outlined in the *BMW of North America, Inc.* v. *Gore,* 116 S. Ct. 1589 (1996)[1] case to reverse or reduce the quantum of punitive damage awards. *Continental Trend Resources, Inc.* v. *OXY USA, Inc.,* 101 F.3d 634, 642 (10th Cir. 1996) ($30 million dollar punitive judgment reduced to $6 million based upon *BMW* showing that the harm "though egregious, was entirely economic, and thus less worthy of punishment than harm to health and safety"); *Patterson* v. *P.H.P. Healthcare*

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[1] For the Court's convenience, copies of all non-California cases are included in the separate Appendix of Non-California cases filed concurrently with this brief.

Corporation, 90 F.3d 927, 943 (5th Cir. 1996) (punitive damages award vacated and remanded for reconsideration in absence of "verbal or physical abuse" or repeated misconduct); *Lee* v. *Edwards,* 101 F. 3d 805 (2d Cir. 1996) (application of *BMW* case resulted in remittitur of $200,000 punitive damages award); *Iannone* v. *Harris,* 941 F. Supp. 403, 415 (S.D.N.Y. 1996) (*BMW* factors mandate reduction of punitive award from $250,000 to $50,000 since conduct while repugnant "was a single incident"); *Management Computer Services, Inc.* v. *Hawkins, Ash, Baptie & Co.,* 1996 Wisc. LEXIS 115, *47 (Wis. Sup. Ct. 1996) ($1.75 million award reduced to $650,000 because, although wrongful and malicious, it only caused only economic injury); *Shippen* v. *Parrott,* 553 N.W.2d 503, 510-11 (Sup Ct. S.D. 1996) (case involved a single incident rather than repeated misconduct mandating reduction from $113,000 to $25,000 punitives). Thus, the courts of the Tenth Circuit, the Fifth Circuit, the Second Circuit, the Southern District of New York, as well as the Supreme Courts of Wisconsin and South Dakota, have all relied upon the reprehensibility issues highlighted by *BMW* to reverse or reduce punitive damages.

As noted, the *BMW* Supreme Court tagged as "[p]erhaps the most important indicium of the reasonableness of a punitive damages award" as "the degree of reprehensibility of the defendant's conduct." *BMW,* 116 S. Ct. at 1599.[2] This is because in reviewing the enormity of an offense "some wrongs are more blameworthy than others." *Id.* The Supreme Court explained that there were certain "aggravating

---

[2] The Court actually highlighted three "guideposts" for evaluating whether punitive damages awards are constitutionally excessive: "Degree of Reprehensibility"; "Ratio [of punitive damages] to the actual harm inflicted on the plaintiff; and "the civil or criminal penalties that could be imposed for comparable misconduct." *Id.* at 1599, 1601, 1603.

However, as already noted, the Court's focus was on reprehensibility, which the Court described as most important. Therefore, it is appropriate to highlight the "aggravating factors" the Supreme Court identified to scrutinize reprehensibility, as did each of the courts cited above which applied the *BMW* case.

factors associated with particularly reprehensible conduct." *Id.* It identified these factors as: (1) whether "a defendant has repeatedly engaged in prohibited conduct while knowing or suspecting that it was unlawful"; (2) whether the harm caused was to the health or safety of individuals or instead purely economic harm; and (3) whether the "target" is "financially vulnerable." *Id.*

Based upon the absence of such aggravating factors in the record before it, the Supreme Court held that a $2 million punitive damage award was grossly excessive under the due process requirements of the Federal Constitution, explaining at page 1601:

> That conduct is sufficiently reprehensible to give rise to tort liability, and even a modest award of exemplary damages, does not establish the high degree of culpability that warrants a substantial punitive damages award. Because this case exhibits none of the circumstances ordinarily associated with egregiously improper conduct, we are persuaded that BMW's conduct was not sufficiently reprehensible to warrant imposition of a $2 million exemplary damages award.

B. California Courts Require A Similar Separate Evaluation Of Reprehensibility, Which Would Reduce Or Overturn This Award.

Reprehensibility or the wrongfulness of the misconduct is likewise one of the three factors which must be considered in evaluating punitive damages under California law. To be justified, a punitive damage award

* * *

two sentence review of the nature of its conduct, followed by a quick affirmance of the award. More is required by common sense as well as the law.

Likewise, the complexity of the facts and the nature of the briefing may have disguised the genuine nature of the issues governing Fireman's Fund's conduct. Certainly, in 1987, it had every reason to legitimately believe that an exposure to covered liability in excess of policy limits was a prerequisite to its duty to settle. This "genuine issue" means that Fireman's Fund's failure to contribute to settlement was not in bad faith.

Dated: January 21, 1997 Respectfully Submitted,

SONNENSCHEIN NATH & ROSENTHAL

By: S/

Paul E.B. Glad
Kelly B. Valen
Cheryl Dyer Berg

Attorneys for Appellant
FIREMAN'S FUND
INSURANCE COMPANY, INC.

PROOF OF SERVICE BY FEDERAL EXPRESS

I am a citizen of the United States. I am over the age of 18 years and not a party to the within action. My business address is 685 Market Street, 10th Floor, San Francisco, California 94105.

On January 21, 1997 I caused to be served by Federal Express at 127 Kearny Street, San Francisco, California copies of **APPELLANT'S PETITION FOR REHEARING** addressed to:

Clerk
California Courts of Appeal
First Appellate District, Division Three
303 Second Street, Suite 600
San Francisco, CA 94107
(Original and Four Copies)

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed on January 21, 1997 at San Francisco, California.

S/ _____
Sandy LeCompte

1ST CIVIL NO.

A06306

In The Court Of Appeal

OF THE

State Of California

FIRST APPELLATE DISTRICT
DIVISION THREE

PAINEWEBBER REAL ESTATE SECURITIES, INC.,
PAINEWEBBER GROUP, INC.,
PAINEWEBBER GROUP, INCORPORATED, and
PAINEWEBBER MORTGAGE FINANCE, INC.,
Plaintiffs and Respondents,

v.

FIREMAN'S FUND INSURANCE COMPANY, INC.,
Defendant and Appellant.

Superior Court of California, County of San Francisco
Case Number 888592
Honorable Anne Bouliane, Judge

APPELLANT'S REPLY TO SUPPLEMENTAL BRIEF

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APPENDIX F

good intention to maintain the program into the summer of 1985 (RSB, at p. 4) does not alter the fact that PaineWebber management had already determined to end the program in mid-March.

PaineWebber cannot rewrite history. The evidence in the record indisputably shows that PaineWebber's interpretation of the "shutdown" letter and affirmative decision to halt further loan referrals caused Homestead's damages and that Homestead's defamation claim was, at most, garnish on its breach of contract claim.

III. THE EXTRAORDINARY PUNITIVE DAMAGE AWARD IS UNJUSTIFIED AND, IN ANY EVENT, EXCESSIVE UNDER *NEAL*.

PaineWebber's punitive damage argument and presentation of *Neal*[1] factors is fraught with misinformation and unproven assumptions which serve only to undermine its position. Rather than burden the Court with arguments previously briefed in Fireman's Fund's Opening and Reply Briefs, Fireman's Fund will focus on the specific points which PaineWebber raises in its Supplemental Brief in an effort to salvage the insupportable punitive damage award.

Fundamentally, PaineWebber's attempt to dilute insurers' federal constitutional protections against excessive punitive damage awards fails to comport with U.S. Supreme Court requirements. (RSB, at pp. 17-19.) The Supreme Court has previously declared that the requirement of due process forbids punitive damage awards "grossly out of proportion to the severity of the offense." *Pacific Mut. Life Ins. Co.* v. *Haslip,* 499 U.S. 1, 22 (1991). In its most recent examination of punitive damages, the Court struck a $2 million punitive damage award as excessive relative to the defendant's conduct, finding the award "tantamount to a severe criminal penalty." *BMW of North America, Inc.* v. *Gore,* 116 S. Ct. 1589, 1604 (1996). In so ruling, the Court instructed that the degree of reprehensibility of a defendant's conduct, one of the three Neal factors, is "[p]erhaps the most important

[1] *Neal* v. *Farmers Ins. Exch.,* 21 Cal. 3d 910 (1978).

indicium of the reasonableness of a punitive damage award." *Id.* at 1599. The Court also held that "[e]lementary notions of fairness . . . dictate that a person receive fair notice not only of the conduct that will subject him to punishment but also of the severity of the penalty that a State may impose." *Id.* at 1598.

PaineWebber fails in its attempt to distinguish *BMW* from this case. (RSB, pp. 18-19.) As in *BMW,* the alleged "harm" to PaineWebber is purely economic and there are no "aggravating factors" such as "deliberate false statements, acts of affirmative misconduct, or concealment of evidence of improper motive." *Id.* at 1599-1601. Moreover, like BMW, Fireman's Fund had "good reason" to believe its conduct lawful and reasonable. Id.; see ARB at pp. 22-29. Like BMW, Fireman's Fund had no "fair notice" that declining to contribute to a settlement, consistent with its contractual rights and in the absence of any evidence of covered damages, would expose it to a punitive damage award more than four times as large as the largest reported award in California history.

A. There Is No Evidence Of Malice.

Fireman's Fund noted in its earlier briefing that the best objective criteria for evaluating the reprehensibility of an insurer's conduct is whether there is "a consistent and unremedied pattern of egregious insurer practices."[2] ARB, p.33 (quoting *Tomaselli* v. *Transamerica Ins. Co.,* 25 Cal. App. 4th 1269, 1287 (1994)). The U.S. Supreme Court adopted the same analysis in *BMW,* holding that "evidence that a defendant has repeatedly engaged in

* * *

[2] Contrary to PaineWebber's distorted analysis, the *Tomaselli* court itself, not Fireman's Fund, suggested that " 'a consistent and unremedied pattern of egregious insurer practices' is *required* in order for the insurer's 'bad faith' conduct to rise to the level of malicious disregard of the insured's rights so as to warrant the imposition of punitive damages." *Tomaselli,* 25 Cal. App. 4th at 1287 (emphasis added; brackets omitted); *see also* ARB, at p. 33.

results that jar one's Constitutional sensibilities." *Pacific Mut. Life Ins. Co.* v. *Haslip,* 499 U.S. 1, 18, 111 S. Ct. 1032, 1043 (1991). A review of the record in this case establishes that the punitive damages awarded by the jury and confirmed by the trial court sufficiently "jar one's Constitutional sensibilities" such that the judgment should not stand.

CONCLUSION

PaineWebber has established nothing more than a legitimate coverage dispute between two sophisticated corporate entities. The utter lack of "clear and convincing" evidence demonstrating malice renders PaineWebber's arguments for "punishment" and "deterrence" hollow and of little relevance in this case. As PaineWebber would have it, insurers would be punished for and "deterred" from legitimately disagreeing with their insureds and asserting their contractual rights. Such punishment, "tantamount to a severe criminal penalty" (*BMW,* 116 S. Ct. at 1604), is not the law. The judgment should be reversed.

Dated: July 3, 1996 Respectfully submitted,

SONNENSCHEIN NATH & ROSENTHAL

By: S/
Paul E.B. Glad

Attorneys for Appellant
FIREMAN'S FUND INSURANCE

PROOF OF SERVICE BY MAIL
Code Civ. Proc. § 1013a(3)

I, Joan Schoenitzer, hereby declare:

I am employed in the City and County of San Francisco, California in the office of a member of the bar of this court at whose direction the following service was made. I am over the age of eighteen years and not a party to the within action. My business address is Sonnenschein Nath & Rosenthal, 685 Market Street, 10th Floor, San Francisco, California 94105. I am personally and readily familiar with the business practice of Sonnenschein Nath & Rosenthal for collection and processing of correspondence for mailing with the United States Postal Service, pursuant to which mail placed for collection at designated stations in the ordinary course of business is deposited the same day, proper postage prepaid, with the United States Postal Service.

On June 20, 1997, I served: **APPELLANT'S REPLY TO SUPPLEMENTAL BRIEF** on the interested parties in this action by placing a true copy thereof, on the above date, enclosed in a sealed envelope, following the ordinary business practice of Sonnenschein Nath & Rosenthal, for collection and mailing in the United States mail addressed as follows:

Clerk
California Supreme Court
Ronald Regan Building
300 South Spring Street,
Second Floor
Los Angeles, CA 90013
(5 copies)

James P. Bennett, Esq.
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1110 Peachtree Street,
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Atlanta, GA 30309-4530

Honorable Ann Bouliane
San Francisco County Superior Court
633 Folsom Street, Room 210
San Francisco, CA 94107-1385

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct, and that this declaration was executed on June 20, 1997, at San Francisco, California.

S/
Joan Schoenitzer

In The Supreme Court
OF THE
State Of California

SUPREME COURT CASE NO._____

PAINEWEBBER REAL ESTATE SECURITIES, INC.,
PAINEWEBBER GROUP, INC.,
PAINEWEBBER GROUP, INCORPORATED, and
PAINEWEBBER MORTGAGE FINANCE, INC.,
Plaintiffs and Respondents,

v.

FIREMAN'S FUND INSURANCE COMPANY, INC.,
Defendant and Appellant.

PETITION FOR REVIEW
OF DECISION OF THE COURT OF APPEAL
FIRST APPELLATE DISTRICT, DIVISION THREE
Appeal Number A063060
San Francisco Superior Court Number 888592

PAUL E.B. GLAD (No. 79045)
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FIREMAN'S FUND INSURANCE COMPANY, INC.

APPENDIX G

conduct was not reprehensible, and certainly cannot support the award of $21 million.

I. EXAMINED IN LIGHT OF THE THREE *BMW* "GUIDEPOSTS," IT IS EVIDENT THAT FIREMAN'S FUND DID NOT RECEIVE ADEQUATE NOTICE OF THE MAGNITUDE OF THE SANCTION THAT CALIFORNIA MIGHT IMPOSE FOR REFUSING TO SETTLE THE *HOMESTEAD* CASE AND THAT THE $21 MILLION PUNITIVE DAMAGE AWARD IS GROSSLY EXCESSIVE.

As the *BMW* decision makes clear, "[e]lementary notions of fairness enshrined in our constitutional jurisprudence dictate that a person receive fair notice not only of the conduct that will subject him to punishment but also of the severity of the penalty that a State may impose." *BMW*, 116 S. Ct. at 1598. In determining whether a punitive damage award is "grossly excessive" and hence constitutionally repugnant, the Supreme Court focused upon three "guideposts": (1) "Degree of Reprehensibility"; (2) "Ratio" of punitive damages to the actual harm inflicted on the plaintiff; and (3) "the civil or criminal penalties that could be imposed for comparable misconduct." *Id.* at 1599, 1601, 1603. Courts nationwide have followed the *BMW* factors to reverse or reduce punitive damage awards.[1]

---

[1] *Continental Trend Resources, Inc.* v. *Oxy USA, Inc.*, 101 F.3d 634, 642 (10th Cir. 1996) ($30 million dollar punitive judgment reduced to $6 million based upon *BMW* showing that the harm "though egregious, was entirely economic, and thus less worthy of punishment than harm to health and safety"); *Patterson* v. *P.H.P. Healthcare Corp.*, 90 F.3d 927, 943 (5th Cir. 1996) (punitive damage award vacated and remanded for reconsideration in absence of "verbal or physical abuse" or repated misconduct); *Lee* v. *Edwards*, 101 F.3d 805 (2d Cir. 1996) (application of *BMW* case resulted in remittitur of $200,000 punitive damage award); *Iannone* v. *Frederic R. Harris, Inc.*, 941 F. Supp. 403, 415 (S.D.N.Y. 1996) (*BMW* factors mandate reduction of punitive award from $250,000 to $50,000 since conduct while repugnant "was a single incident"); *Geuss* v. *Pfizer, Inc.*, 1996 U.S. Dist. LEXIS 18784, *38-40 (E.D.Pa. 1996) (noting that

Although informed of the recent *BMW* decision, the Court of Appeal completely ignored it. It likewise ignored California cases emphasizing similar objective criteria for evaluating reprehensibility. Measured against the *BMW* guideposts and these objective criteria, it is clear that the $21 million punitive damage award cannot pass constitutional muster.

A. Degree of Reprehensibility

"Perhaps the most important indicium of the reasonableness of a punitive damages award is the degree of reprehensibility of the defendant's conduct." *Id.* at 1599. This is because "some wrongs are more blameworthy than others." *Id.* The "aggravating factors associated with particularly reprehensible conduct" identified by the Supreme Court included: (1) whether " a defendant has repeatedly engaged in prohibited conduct while knowing or suspecting that it was unlawful"; (2) whether the harm caused was to the health or safety of individuals or instead purely economic harm; and (3) whether the "target" is "financially vulnerable." *Id.*

California courts in the past have likewise struggled to identify objective factors by which to evaluate excessiveness of punitive damages. These factors are similar to those identified in *BMW*. Thus, California courts consider whether the misconduct was repeated or a corporate policy affecting multiple individuals. *Tomaselli* v. *Transamerica Ins. Co.*, 25 Cal. App. 4th 1269, 1287 (1994); *Mock* v. *Michigan Millers Mut. Ins. Co.*, 4 Cal. App. 4th 306, 329 (1992).

"there was no evidence that [the defendant] has a propensity to engage in future" misconduct, the court reduced $150,000 in punitive damages to $17,500); *Management Computer Services, Inc.* v. *Hawkins, Ash, Baptie & Co.*, 1996 Wisc. LEXIS 115, *47 (Wis. Sup. Ct. 1996) ($1.75 million award reduced to $650,000 because, although wrongful and malicious, defendant's misconduct caused only economic injury); *Shippen* v. *Parrott*, 553 N.W.2d 503, 510-11 (Sup. Ct. S.D. 1996) (citing *BMW* for its holding that "punitive damages may not be imposed to 'punish' or to 'deter' nonactionable conduct," court reduced punitive award from $113,000 to $25,000).

Indeed, the California Supreme Court has held that the "principal purpose" of punitive damages is to "discourage the perpetuation of objectionable corporate policies." *Egan* v. *Mutual of Omaha Ins. Co.*, 24 Cal. 3d 809, 820 (1979), *cert. denied*, 445 U.S. 912 (1980). *See also Downey Savings & Loan Ass'n* v. *Ohio Casualty Ins. Co.*, 189 Cal. App. 3d 1072, 1099 (1987) (Justice Kennard explaining that punitive damages were not excessive, as the jury "could have reasonably intended to punish [the insurer] not only for its reprehensible conduct towards [the insured] but also for its invidious practices [in many different cases], thereby discouraging a repeat thereof").

Further, courts consider whether the plaintiff is a sophisticated entity or a vulnerable consumer. *Slottow* v. *American Cas. Co.*, 10 F.3d 1355, 1361 (9th Cir. 1993) (applying California law). Finally, courts consider whether the case involves purely economic harm or a threat to health or safety. *Wollersheim* v. *Church of Scientology*, 212 Cal. App. 3d 872, 907 (1989).

None of these "aggravating factors" was analyzed by the trial court or appellate court in this case. None are in fact present. This was a case of an isolated, individual dispute involving a single claim. The only harm allegedly caused by Fireman's Fund's conduct was economic. And finally, the "target" is not "financially vulnerable"—it is a large, sophisticated corporation "with the financial resources to weather . . . sharp business practices." *Las Palmas Associates* v. *Las Palmas Center Associates*, 235 Cal. App. 3d 1220, 1255 (1991).

Although the Court of Appeal states that Fireman's Fund's conduct was "egregious" because "it completely disregarded the long-established law" (Opinion, p. 26), the reality is that Fireman's Fund's conduct was based upon a good faith belief that it had a contractual right to do precisely what it did based upon California case law which the Court of Appeal ignored. In light of *Doser*, 101 Cal. App. 3d

883 (as reaffirmed in *Finkelstein*, 11 Cal. App. 4th 926), Fireman's Fund "could reasonably interpret [that case] as establishing safe harbors" of acceptable insurer conduct. *BMW*, 116 S. Ct. at 1600. "To punish a person because he has done what the law plainly allows him to do is a due process violation of the most basic sort." Id. at 1597-98, n.19 (quoting *Bordenkircher* v. *Hayes*, 434 U.S. 357, 363 (1978)).

But even if Fireman's Fund's interpretation of the existing law were wrong, an erroneous but not unreasonable interpretation of its contractual rights could not constitute sufficiently reprehensible conduct to justify a $21 million punitive damage award. "That conduct is sufficiently reprehensible to give rise to tort liability, and even a modest award of exemplary damages, does not establish the high degree of culpability that warrants a substantial punitive damages award." *BMW*, 116 S. Ct. at 1601.

B. Ratio

The *BMW* Court also endorsed the proposition that "a comparison between the compensatory award and the punitive award is significant." Id. at 1602. The Court rejected a "categorical approach" of drawing "a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable. . . ." *Id.* The "proper inquiry" is " 'whether there is a reasonable relationship between the punitive damages award and the harm likely to result from the defendant's conduct as well as the harm that actually has occurred.' " *Id.* (*quoting TXO Production Corp.* v. *Alliance Resources Corp.*, 509 U.S. 443, 460 (1993) (quotation marks, citation and emphasis omitted)).

A 7 to 1 ratio might be appropriate under *BMW* analysis if misconduct had resulted in nominal injury to a large number of people. But a 7 to 1 ratio cannot be appropriate where, as here, a single plaintiff is awarded $3,000,000 compensatory damages for the handling of a single claim. *Id.* at 1599.

Nor is there a "reasonable relationship" between the $21 million and the "harm likely to result from the defendant's

conduct as well as the harm that actually occurred." *Id.* at 1602 (quotation marks, citation and emphasis omitted). Here, if the case had gone to judgment and *covered* damages for defamation had been awarded in excess of the policy limits, Fireman's Fund would in all likelihood have been responsible for that excess judgment. *Camelot by the Bay,* 27 Cal. App. 4th at 46. As a matter of law, Fireman's Fund was *not* required to take PaineWebber's potential exposure to *non*-covered damages into account when it considered PaineWebber's negotiated settlement. *Id.* at 52. As a result, PaineWebber faced no potential "harm" from Fireman's Fund's refusal to participate in that settlement.

Nor did any harm actually occur. Despite Fireman's Fund's refusal to participate, the settlement was consummated anyway. PaineWebber was able to accomplish exactly what it wanted: it avoided the possibility of a large, non-covered judgment.

All of these factors taken together strongly suggest that the high 7 to 1 ratio here "must surely 'raise a suspicious judicial eyebrow.'" *BMW,* 116 S. Ct. at 1603 (*quoting TXO,* 509 U.S. at 482).

C. Sanctions for Comparable Misconduct

BMW's fair notice requirement makes it essential to compare punitive damage awards with "the civil or criminal penalties that could be imposed for comparable misconduct." *Id.* The statutory penalties a State imposes for comparable misconduct are significant, because "a reviewing court engaged in determining whether an award of punitive damages is excessive should 'accord "substantial deference" to legislative judgments concerning appropriate sanctions for the conduct at issue.'" *Id.* (*quoting Browning-Ferris Industries of Vt., Inc.* v. *Keloc Disposal, Inc.,* 492 U.S. 257, 301 (1989) (O'Connor, J., concurring and dissenting) (quotation marks and citation omitted)).

Here, the maximum statutory penalty for insurance bad faith is $10,000. California Insurance Code § 790.035. Even willful violation of a cease and desist order risks a maximum

penalty of only $55,000. California Insurance Code § 790.07. The California legislature evidently had concluded that a million dollar award is *unnecessary* to deter even intentional bad faith conduct. $21 million is *not* needed to get the message across.

D. *BMW* Raises Substantial Doubt About California's Current Emphasis on Net Worth

California case law has traditionally included in its triparte analysis of the propriety of punitive damages the defendant's net worth. *See e.g., Neal* v. *Farmers Ins. Exchange,* 21 Cal. 3d 910, 928 (1978). The rationale for this approach is, presumably, that a bigger penalty is necessary to deter a more financially prosperous defendant. The Court of Appeal here focused almost exclusively on Fireman's Fund's large net worth in justifying the size of the $21 million punitive award. This limited focus is improper under California law. The California Supreme Court has held that a defendant's ability to pay, in and of itself, cannot justify a "multimillion dollar award," and that, while ability to pay may serve as a limitation on punitive damages, all objective factors enunciated by California courts must be considered. *Adams* v. *Murakami,* 54 Cal. 3d 105, 111 & n.2 (1991).

While a defendant's *inability* to pay is relevant, a substantial net worth does not mean that a huge punitive damage award is appropriate. Indeed, where net worth is substantial, this factor would appear to have little or no relevance under the guidance of *BMW. BMW* notably does not make financial condition one of its three guideposts. More significant is what *BMW* does say about the significance of a defendant's financial condition and the state's interest in deterrence. The *BMW* Court rejected the suggestion that large punitive damages are appropriate to "prompt[] a change in [BMW's] policy." 116 S. Ct. at 1603. Implicit in that argument was the notion that BMW, as a large corporation, needed a large award to deter its misconduct. But the Court made clear that BMW's change in policy "sheds no light on the question whether a lesser deterrent would have adequately protected" the state's interest in deterrence. *Id.* What matters is

effective deterrence, not merely the financial condition of the defendant. The question is whether "a more modest sanction would not have been sufficient. . . ." *Id.*

As in *BMW,* the "sanction imposed in this case cannot be justified on the ground that it was necessary to deter future misconduct without considering whether less drastic remedies could be expected to achieve that goal." *Id.* The Court of Appeal gave no consideration to whether less drastic remedies could achieve the goal of deterrence. It simply concluded that since Fireman's Fund had a large net worth, a staggering award was appropriate. But "[t]he fact that [Fireman's Fund] is a large corporation rather than an impecunious individual does not diminish its entitlement to fair notice of the demands that [California] impose[s] on the conduct of its business." *Id.* at 1604.

BMW's failure to make net worth a "guidepost" against which to test the excessiveness of punitive damages is consistent with prior California law. That case law holds that, to be justified, a punitive damage award must fully satisfy *each* of several objective criteria, and that ability to pay, in and of itself, cannot be used to justify a "multimillion dollar award." *Adams* v. *Murakami,* 54 Cal. 3d 105, 111 & n.2 (1991); *accord Pulla* v. *Amoco Oil Co.,* 72 F.3d 648, 659 n.16 (8th Cir. 1995) ("While a defendant's wealth may be taken into account in order to ensure that an award will adequately deter any future such conduct, a defendant's wealth cannot alone justify a large punitive damages award.").

"[T]he key question before the reviewing court is whether the amount of damages exceeds the level necessary to properly punish and deter." *Adams,* 54 Cal. 3d at 110 (quotation marks and citation omitted). To be sure, a $21 million dollar award sends a forceful message. But so does an award of $5 million or $1 million. The rule is that the *least* amount that sends a forceful message is acceptable, not that *any* amount which sends a forceful message is acceptable.

> The fact that a multimillion dollar penalty prompted a change in policy sheds no light on the question whether a lesser deterrent

> would have adequately protected the interests of Alabama consumers. In the absence of a history of noncompliance with known statutory requirements, there is no basis for assuming that a more modest sanction would not have been sufficient to motivate full compliance. . . . *BMW,* 116 S. Ct. at 1603.

For example, in *Las Palmas,* 235 Cal. App. 3d at 1255, where the punitive award was against a defendant whose net worth was nearly $500 million, the Court of Appeal reduced the award from $10 million to $2 million and explained:

> [W]e believe a $2 million award still sends a forceful message to sellers that they cannot fraudulently induce parties to enter into agreements without penalty. Besides punishing sellers, the award also acts as a deterrent against future misconduct. Although sellers have a combined net worth of nearly a half billion dollars, they will no doubt think twice before fraudulently entering into another contract.

Similarly, in *Grimshaw* v. *Ford Motor Co.,* 119 Cal. App. 3d 757 (1981), the jury awarded $125 million in punitive damages, which was remitted to $3.5 million. Id. at 771-72. Even though the defendant's net worth was $7.7 billion and its net income was $983 million, the Court of Appeal said $3.5 million was not "so small that it can be simply written off as a part of the cost of doing business. . . ." *Id.* at 820.

In short, Fireman's Fund has a right to a meaningful review of the punitive damage award which considers whether the degree of Fireman's Fund's reprehensibility justifies the size of the award. There are objective factors recognized by both the United States Supreme Court and the courts of California which are intended to focus this review. Application of these factors here would mean at a minimum a substantial reduction of the punitive award.

* * *

the $21 million punishment subsequently awarded by the jury and affirmed by the Court of Appeal. Indeed, under the Supreme Court's recent holding in *BMW,* Fireman's Fund's actions in this isolated incident *cannot* support such a huge award.

This Court should grant review in order to clarify the objective criteria against which to judge the reprehensibility of conduct, and thus the excessiveness of punitive damage awards. Further, this Court should grant review to provide California courts with guidance as to the rights and obligations of excess carriers when there is *some* exposure to covered damages, but *great* potential exposure to *un*covered damages. Finally, this Court should grant review to explain the applicability of the "genuine legal issue" doctrine in cases, such as this, in which unsettled law leads an insurer to a course of action which may ultimately prove incorrect.

Dated: February 13, 1997

Respectfully submitted,

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PROOF OF SERVICE BY MAIL

I am a citizen of the United States and employed in the City and County of San Francisco. I am over the age of 18 years and not a party to the within action. My business address is 685 Market Street, 6th floor, San Francisco, California 94105.

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S/ _____

Sandy LeCompte